2018 INTEGRATED REPORT & FINANCIAL STATEMENTS

Family Bank
With you, for life

FAMILY BANK LIMITED

INTEGRATED REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018

FamilyBank
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ABOUT THE INTEGRATED REPORT AND AUDITED FINANCIAL STATEMENTS 2018

Family Bank Limited is pleased to present its annual Integrated Report, which covers the period from 1 January 2018 to 31 December 2018. This report contains comprehensive information of our financial performance, stakeholders, governance, material issues, risks and opportunities and how these influence our strategic initiatives. In this report, Family Bank demonstrates how we create and sustain value through our business.

This report is compiled and presented in accordance with the Corporate Governance Guidelines and Codes of Conduct prescribed by the Central Bank of Kenya, the Corporate Governance Guidelines of the Capital Markets Authority (CMA), the Continuing Listing Obligations of the CMA as required by the Nairobi Securities Exchange and the Global Reporting International (GRI).

We have implemented the framework as far as practical and our approach to integrated reporting will continue to evolve over time, in line with the framework.

Our Annual Financial Statements were prepared in accordance with International Financial Reporting Standards (IFRS) and the requirements of the Companies Act, 2015. We received external assurance from our auditor, PWC Kenya on the fair presentation of these annual financial statements. See the Independent Auditor's Report on pages 47 to 50.

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Family Bank Vision, Mission and Core Values

Family Bank at Glance

Our Vision

To be the financial institution that leads in the positive transformation of people's lives in Africa.

Our Mission

We positively transform people's lives by providing quality financial services through innovative, efficient and reputable practices

Our Values

Winning Together – Within ourselves and with our customers, we work together and we win together
Self Belief – In ourselves and our customers' ability to change the world
Transparency – Our customers will trust and reward us for it
Humility – It's not about us, it's about our customers

Our Purpose

To enable people create and sustain wealth through access to flexible, affordable financial services.

Our Tagline

Our positioning is best captured in our tagline and expresses the promise to our customers in the simplest way.
"With you, for life"

SUBSIDIARY

FAMILY BANK INSURANCE AGENCY LIMITED

Family Bank Insurance Agency Limited (FBIA), a fully-fledged subsidiary of Family Bank Limited, was established in 2008. The Insurance Agency is licensed by the Insurance Regulatory Authority (IRA) since May 2010. In the ten years since its establishment, the Agency has recorded an impressive growth year-on-year, attaining a Gross Written Premium (GWP) of KES 850 Million as at December 2018, mainly from its General, Life and Medical insurance businesses. This growth is attributed to improved customer experience, technological innovations in underwriting & distribution and new products.

FBIA is a leading provider of risk management & insurance brokerage solutions. It has more than 50 members of staff, adequately experienced and qualified to handle your insurance and risk management needs with representation in over 90 branches across the country.

The Agency's main objective is to address the insurance needs of Kenyans across the wide economic strata. Through partnerships with reputable insurance companies in the industry, FBIA offers a full bouquet of innovative insurance products and services using the Bancassurance model. Bancassurance is the provision of insurance and banking products and services, through a common distribution channel and to the same client base.

The Agency also facilitates access to professional insurance advisory services and also avails convenient and accessible insurance policies and claims service by our customers through the wide branch outreach and alternative banking channels.

OUR SERVICES

- Advisory Insurance services on General, Marine, Agriculture and Medical insurance policies
- Life Assurance products for groups and individuals
- Group and Staff medical scheme administration services
- Claims Management
- Insurance Premium Financing

All these services and products are offered through an integrated and robust Banc assurance IT system to ensure that insurance business is well served and all branches are well connected to enhance efficiency of service delivery across the country.

THE COMPANIES ACT 2015

FAMILY BANK LIMITED

ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the **12TH ANNUAL GENERAL MEETING** of the shareholders will be held at **KENYATTA INTERNATIONAL CONFERENCE CENTRE AMPHITHEATRE** on Thursday 30th May 2019 at 10:00 am to transact the following business:

Ordinary Business:

1. To receive, consider and if thought fit, adopt the Integrated Report, the Audited Financial Statements for the year ended 31st December, 2018, together with the Chairman's, Directors' and Auditors' reports thereon.

2. To consider and if deemed fit, approve the recommendation of the Board that there shall be no dividend paid for the year ended 31st December 2018.

3. Resignation, Rotation and Election of Directors in accordance with Article 112 of the Articles of Association:

   3.1 Mr. L. Tiampati retires by rotation and being eligible, offers themselves for appointment in accordance with section 132 of the Companies Act.

   3.2 Dr. W. Kiboro retires by rotation and being eligible, offers themselves for appointment in accordance with section 132 of the Companies Act.

   3.3 Dr. W. Kiboro, a Director and Chairperson to the Board, having attained the age of seventy years retires from office by rotation and, in terms of Clause 2.5 of the Capital Markets Code of Corporate Governance Practices for Issuers of Securities to the Public 2015, offers himself for re-election.

4. To receive, consider and if thought fit approve the Directors' remuneration for the year ending 31st December 2018.

5. To approve that the auditors PricewaterhouseCoopers (PwC), being eligible and having expressed their willingness, will continue in office in accordance with section 721 of the Companies Act, No. 17 of 2015 and to authorize the directors to fix their remuneration.

Special Business:

6. To consider and if thought fit pass the following resolution as a special resolution, as recommended by the Directors:

"That the name of the Company be and is hereby changed from "Family Bank Limited" to "Family Bank PLC" in compliance with Section 53 of the Companies Act, 2015 and with effect from the date set out in the Certificate of Change of Name issued in that regards by the Registrar of Companies".

By order of the Board

Company Secretary

Nairobi

30th April 2019

Notes: A member entitled to attend and vote at this Meeting may appoint a proxy to attend and vote on his/her behalf and such proxy need not be a member of the Company. The proxy shall be required to be deposited at the Company Secretary office 8th Floor at Family Bank Towers Muindi Mbingu Street Nairobi not less than forty-eight hours before the time for holding the meeting failing which it shall be invalid. In the case of a corporate body the proxy must be under its common seal. The proxy form is available on the Company's website www.familybank.co.ke

The full set of audited accounts for the year ended 31st December 2018 is available at the Company's registered office at Family Bank Towers 6th Floor, Muindi Mbingu Street Nairobi or can be downloaded at the website **www.familybank.co.ke**

CORPORATE INFORMATION

DIRECTORS

Non-Executive

Dr. Wilfred D. Kiboro- Chairman
Mr. Titus K. Muya
Dr. Ruth Waweru
Mr. Lazarus Muema
Mr. Lerionka S. Tiampati
Mr. Francis Gitau Mungai

COMPANY SECRETARY

Rebecca Mbithi
Certified Public Secretary (Kenya)
8th Floor, Family Bank Towers,
Muindi Mbingu Street
P.O. Box 74145 - 00200, Nairobi
Tel: 254-2-318173/318940/2/7/0720 098 300
Fax: 254-2-318174
Email: info@familybank.co.ke
Website: www.familybank.co.ke

REGISTERED OFFICE

Family Bank Limited
6th Floor, Family Bank Towers, Muindi Mbingu Street
P.O. Box 74145- 00200, Nairobi
Tel: 254-2-318173/318940/2/7/0720 098 300
Fax: 254-2-318174
Email: info@familybank.co.ke
Website: www.familybank.co.ke

AUDITOR

PricewaterhouseCoopers Kenya
Certified Public Accountants
PWC Tower, Waiyaki Way/Chiromo Road, Westlands
P.O. Box 43963-00100
Nairobi, Kenya

LEGAL ADVISERS

Mboya Wangong'u & Waiyaki Advocates
Lex Chamber, Maji Mazuri Road
Off James Gichuru Road
Nairobi

CORPORATE INFORMATION

CORRESPONDENT BANKS

Deutsche Bank AG London
6 Bishopsgate
London
EC2P 2AT
United Kingdom

DZ Bank AG
60265 Frankfurt am Main

Deutsche Bank Trust Company Americas
P O Box 318, Church Street Station
New York, New York 10008 – 0318

National Bank of Canada
P.O. Box 600 rue de la Gauchetière Ouest
Montréal, Québec, Canada

BOARD COMMITTEES

Credit Committee

Mr. Francis Mungai - Chairman
Mr. Titus K. Muya
Dr. Wilfred D. Kiboro

Audit Committee

Mr. Lazarus Muema - Chairman
Dr. Ruth Waweru
Mr. Lerionka S. Tiampati

Risk Management and Compliance Committee

Mr. Lazarus Muema - Chairman
Dr. Ruth Waweru
Mr. Lerionka S. Tiampati

Human Resource Committee

Dr. Ruth Waweru - Chairperson
Mr. Titus K. Muya
Dr. Wilfred D. Kiboro
Mr. Francis Mungai

Strategy Committee

Dr. Ruth Waweru - Chairperson
Mr. Titus K. Muya
Mr. Lerionka S. Tiampati
Dr. Wilfred D. Kiboro

Nomination Committee

Dr. Ruth Waweru - Chairperson
Dr. Wilfred D Kiboro
Mr. Titus K. Muya

BOARD OF DIRECTORS

Sitting (L-R): Rebecca Mbithi; Dr. Wilfred Kiboro; Dr. Ruth Waweru Standing (L-R): Titus K. Muya; Francis Gitau Mungai; Lerionka S. Tiampati; Lazarus Muema

BOARD OF DIRECTORS

Dr. Wilfred D. Kiboro
Chairman

Dr. Kiboro holds a Bachelor of Science (Civil Engineering) from the University of Nairobi and he began his engineering career with Shell and Esso where he rose through the ranks to head the Sales and Marketing function. He was later appointed as Managing Director of Rank Xerox, and he is the immediate former Chief Executive Officer of the Nation Media Group where he still serves as Chairman. Dr. Kiboro is also the Chancellor of Riara University and a Trustee of the Rhino Ark, a charitable trust founded in 1988 to support conservation in Kenya and the Chairman Wilfay Investment Limited and Africa Digital Network Limited.

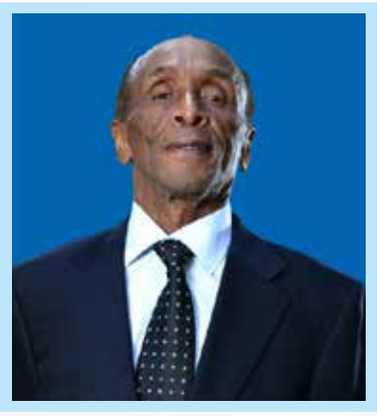
Dr. Kiboro has received various accolades including being a Member of International Who's Who of Professionals, and he is a past Chairman of several organisations including the Media Owners Association, the East African Business Council, the International Press Institute Board, the Federation of Kenyan Employers, and the Standard Chartered Bank, Kenya.

He has also served on the Boards of the Kenya Association of Manufacturers, and the National Environmental Management Authority (NEMA) and East African Breweries Limited among others.

Dr. Ruth Waweru
Vice Chairperson

Dr. Waweru holds a Bachelor of Education from Kenyatta University, an MBA from University of Nairobi and a Doctorate Degree in Business Administration from Nelson Mandela Metropolitan University in South Africa. She is a professional consultant in various facets such as: strategy formulation, organizational development, human resource management and research. Ruth has provided consultancy services to corporations, private sector, national governments and bilateral organizations including the World Bank and the European Union. She has provided services in many African countries such as South Africa, Ethiopia, Uganda, Tanzania and the Republic of South Sudan.

Ruth's experience has seen her transition from managerial roles at the Kenya Institute of Management to heading Liaison Consulting Limited where she is the Chief Executive Officer. She serves in the boards of Oikocredit International, Partners Worldwide, Kenya Orient Life Assurance Limited and All Africa Conference of Churches and is Founder Director of Brookhurst International School.



Mr. Titus K. Muya
Director

TK, as he is popularly known, founded Family Bank in 1984 and he served as the institution's Chief Executive Officer from 1984 to June 2006 after which he chaired the Banks Board of Directors until December 2012. He is one of Kenya's leading visionary entrepreneurs associated with various companies including Kenya Orient Insurance Limited, Daykio Plantations Limited and Alpha Africa Asset Managers Limited on whose Boards he sits or is represented in different capacities.

In recognition of his entrepreneurship and, more specifically, his contribution to the banking industry, TK was awarded the national accolade, Elder of the Order of the Burning Spear, in December 2011.

Mr. Francis Gitau Mungai
Director

Mr. Gitau holds a Masters Degree in Architecture and Urban Design from the University of California, Los Angeles (UCLA) and a Bachelor of Architecture degree, First Class Honours from the University of Nairobi. He is also a Fellow of the Architectural Association of Kenya (FAAK) and is registered by the Board of Registration of Architects & Quantity Surveyors (BORAQS) in Kenya. He is the founding Partner of Aaki Consultants, Architects and Urban Designer and has worked as an Architect with prominent firms like Triad Architects in Nairobi and Urban Innovation Group (UIG) in Los Angeles.

He has vast experience spanning over 30 years and has been a Chairman of various bodies such as the Architectural Association of Kenya (AAK), Kenya Private Sector Alliance (KEPSA) where he was Director and Chairman of Building and Infrastructure Board. Mr. Gitau is the Chairman of the Board of Directors of National Housing Corporation. He is a former lecturer at the University of Nairobi, Architecture and Building Sciences Department where he focused on both Architectural and Urban Design Studios, as well as Professional Practices and management.

Mr. Lerionka S. Tiampati
Director

Mr. Tiampati holds a postgraduate degree (MSc.) in Marketing and Product Management from the Cranfield Institute of Technology (Cranfield University) in the United Kingdom, a diploma of the Chartered Institute of Marketing (DIPM) from the United Kingdom and undergraduate degree in Business Administration (B.Com) from the University of Nairobi. He is the Managing Director & Chief Executive Officer of Kenya Tea Development Agency Holdings Limited.

Prior to taking up his current role, he was the Chief Executive Officer of the Kenya Tea Packers Limited (KETEPA). He previously worked as the Head of Marketing at the Standard Chartered Bank, Marketing Development Manager at Magadi Soda Company and Head of Marketing at the Agricultural Development Corporation. Mr. Tiampati sits on the board of the East Africa Tea Trade Association, The Standard Group and a number of KTDA subsidiary companies. He also holds the national distinction, Moran of the Order of the Burning Spear.

Mr. Lazarus Muema
Director

Mr. Lazarus Muema was appointed to the Family Bank Board in 2017. He is a highly respected professional in the finance sector with experience spanning over 30 years, having held senior positions in multinational corporations both in Kenya and Europe . He has been a Finance Manager at Shell Exploration Kenya and Shell Uganda, a financial controller at Kenya Shell and a finance advisor at Shell International in London, rising through the ranks to the position of the Pensions Investment and Policy Advisor for Africa by the time he left in 2011. Currently, he is a Pension Consultant with Penplan Services Limited, a Pensions Consultancy firm founded in 2011. His expertise is in designing end of Service Benefit Schemes, negotiating end of service packages and formulating Investment Strategies for Pension Schemes.

Mr. Muema holds a Bachelor of Commerce Degree from the University of Nairobi and a Certified Public Accountant (CPAK). He is a board member in various companies including Kenya Orient Insurance Company and East African Gasoil Company. He is also a former Chairman of the Association of Retirement Benefits Schemes of Kenya, Bright Technologies Ltd and Nanga Investments Ltd.

Rebecca Mbithi
Company Secretary and Director Legal Services

Rebecca Mbithi is a seasoned professional and a respected lawyer with extensive leadership background in various organizations, having previously worked at Kenya Tea Development Agencies (KTDA) where she served as Head of Legal and Regulatory Affairs and Rift Valley Railways where she served as the Company Secretary and Legal Counsel. She has vast domain expertise and knowledge in Law, Project Finance, Corporate Restructuring, Equity/Debt Raising and Governance, and has served in the Corporate Governance and Standards Committee of the Institute of Certified Public Secretaries Kenya.

Ms. Mbithi joined Family Bank in January 2015, taking on the role of Company Secretary and Director, Legal Services where she has been instrumental in Strategy and Business Development, Capital and Debt Raising, Risk Management, Compliance and Controls, providing legal services and strengthening the Bank's Governance structures.

Rebecca holds a Masters in Business Administration with a concentration in Strategic Management from United States International University-Africa and an LL.B degree from the University of Nairobi. She is a Certified Public Accountant and a member of the Institute of Certified Public Accountants of Kenya (ICPAK), a Certified Secretary and a Member of the Institute of Certified Secretaries, an advocate of the High Court of Kenya and a member of the Law Society of Kenya. In addition, Rebecca is also a Certified Executive Coach.

CHAIRMAN'S STATEMENT

Dear Shareholders,

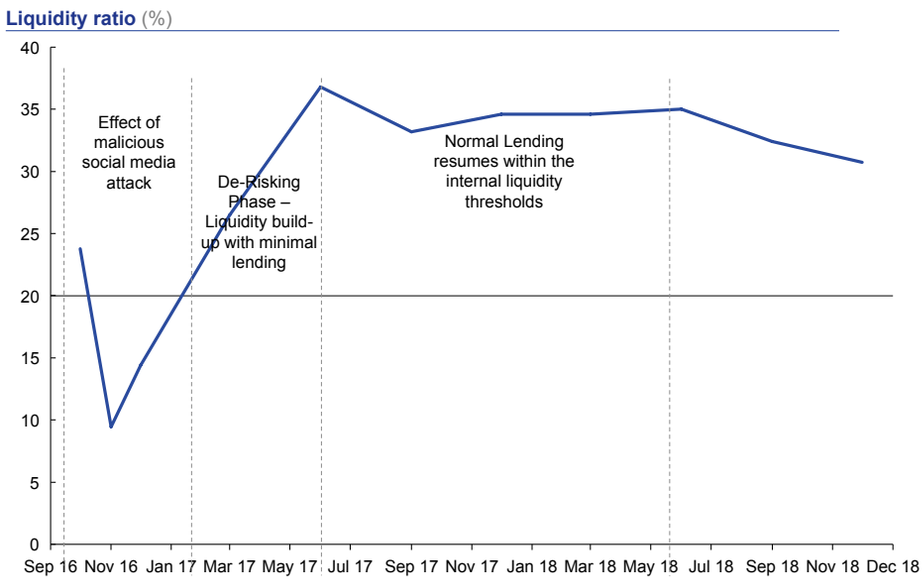
I am pleased to present the Integrated Report and Financial Statements for the year ended 31st December 2018. Our aggressive investment in technology and our aggressive approach in driving efficiencies resulted in a remarkable turnaround for the Bank and registered consistent growth throughout the year.

Key Financial Performance Highlights

- We realized a Profit Before Tax (PBT) of KES 435 Million, reversing a KES 1.36 Billion loss recorded in 2017.
- Customer deposits grew by 2.4% to KES 48.5 Billion in 2018 compared to KES 47.4 Billion in 2017.
- Total non-interest income grew by 15% from KES 2.17 Billion in 2017 to close at KES 2.50 Billion.
- We registered a KES 1.35 Billion reduction in operating costs, translating to a 19% saving relative to the 2017 financial year.
- Staff costs decreased by 20% to KES 1.86 Billion from KES 2.34 Billion recorded in 2017.
- We posted a 17% reduction in loan loss provisions to KES 771.9 Million.
- Net liquid assets closed at 30.7% of deposits from customers as at 31st December 2018, significantly above the CBK mandated minimum of 20%. The full year average liquidity ratio was 33%.

Review of the Macroeconomic Environment

Liquidity has been relatively stable throughout 2018 at levels above 30%



Global Economy

The global GDP growth in 2018 stood at 3% and is expected to slow down to 2.9% in 2019 as a result of moderation in international trade and investments, elevated trade tensions and tightening financial conditions, according to the World Bank's Global Economic Prospects report.

Overall, Global economic activity slowed down in 2018 as result of a confluence of factors affecting the World's major economies. While the US economy experienced a growth of 2.9%, mostly driven by domestic demand, it was weighed down by the negative effects of the trade conflicts with China and the Eurozone, as well as a weaker outlook for some key markets especially Brazil and the UK. The Trump administration's USD 1.5 Trillion tax cut package and its accommodative fiscal and monetary stances, have however boosted consumer spending and consequently supported business and investment in the US.

In the Eurozone, economic growth slumped to a four year low in Q3'2018, as GDP expanded by 0.2%, as a result of reduced exports in the region, increased geopolitical tensions and a slowdown in business activity.
China's growth slightly declined from 6.7% in 2017 to 6.6% in 2018, following a combination of needed regulatory tightening to rein in shadow banking and an increase in trade tensions with the United States.

The Sub-Saharan Africa region remained on a recovery path, with a real regional GDP growth of 3.0% in 2018 as compared to a growth of 2.9% in 2017, according to the Economic survey 2019 by the Kenya National Bureau of Statistics. In East Africa, a rebound was recorded in Rwanda, Uganda, and Kenya driven by improved agricultural performance in the wake of easing drought conditions.

Local Economy

Kenya National Bureau of Statistics (KNBS) in the Economic Survey 2019, estimated that Kenya's real Gross Domestic Product (GDP) grew by 6.3% in 2018, compared to an average growth of 4.9% in 2017. The improved growth is attributable to a stable macroeconomic environment, driven by a recovery in agriculture, accelerated manufacturing activities, sustained growth in transportation, vibrant service sector activities and improved consumer confidence.

The World Bank Doing Business Report 2019, showed that Kenya improved by 19 positions in the global ranking on ease of doing business, from position 80 to position 61. There was also increased output in the real estate, manufacturing, and wholesale & retail trade sectors, which grew by 5.8%, 3.2% and 6.8% respectively.

Banking Sector Developments

Acquisitions and mergers were the top conversation drivers in the banking sector; as evidenced by State Bank of Mauritius (SBM) Bank Kenya's completion of the acquisition of some assets and liabilities of Chase Bank Limited, which was under receivership. Central Bank of Kenya accepted a binding offer from KCB Group, for the acquisition of Imperial Bank Kenya Limited which was under receivership. Commercial Bank of Africa (CBA) Group and NIC Group PLC also communicated their intent to merge their businesses, subject to approval from the relevant regulatory bodies such as Capital Markets Authority (CMA), CBK and other stakeholders.

Due to the effect of the Banking Amendment Act (2015), the sector has reinvented itself and diversified its sources of income into new segments to support and improve the bottom line. Across the sector, the contribution of Non-Funded Income to the total operating income has continued to rise. This non funded income is generated from alternative channels which include mobile banking, agency banking and internet banking as well as fees and commissions, treasury and trade finance income.
With the rise of technology and innovation, the sector has experienced an increase in fraud and cyber security risks. This has brought about the need for banks to invest in risk systems and processes and tighten their compliance policies and procedures.

Regulation remains a key consideration in the banking sector, and it continues to inform key decisions and strategies amongst the various players. Regulation in the sector has increasingly been centred on consumer protection and promoting prudence in the financial services sector.

In September 2018, The National Assembly voted to retain the cap on loans in the Finance Act 2018, effectively retaining the 4.0% cap above the Central Bank Rate (CBR) on interest chargeable on loans. However, the regulation setting the floor of interest payable on deposits at 70.0% of the CBR, was removed. With the removal of the same, banks have adjusted accordingly, with various players indicating a lowering of their interest expense requirements, and a possible improvement in the Net Interest Margin, whose benefits will be fully realized in 2019.

2018 was also the year that the IFRS 9 was implemented and this necessitated banks to review their business models and credit policies, as well as align their strategic objectives. This resulted in stringent lending policies that led to increased preference for collateral-based lending and a widespread review of banks' lending matrices.

The Central Bank of Kenya's guidelines and regulations on Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT), and the Proceeds of Crime and Anti-Money Laundering Act 2009 were enhanced to regulate high-value transactions. Following this move, the Kenya Bankers Association developed guidelines for adoption by member banks which require proper identification of the source of funds for transactions above KES 1 Million and a three-day notice for over the counter transactions exceeding KES 10 Million.

The Central Bank of Kenya also proposed to introduce a Banking Sector Charter that will guide service provision in the sector with an aim to facilitate a market-driven transformation of the Kenyan banking sector and increase access to affordable financial services for the unbanked and under-served population.

INDUSTRY HIGHLIGHTS

The economy and banking sector faced a number of challenges

Area	Themes	Detail
Macro	Slowdown in growth of domestic demand	▪ **Slow growth in the SME and Micro sectors** due to the current credit market conditions adversely impacted the growth of the domestic market.
Industry specific	Changes in Regulation	▪ The adoption of **IFRS 9 model**. The model seeks to improve credit risk provisioning by reporting institutions. Banks will have to not only recognize incurred credit losses but also losses that are expected in future, which adversely affects Bank's profitability.
	Commercial Bank Interest Rates	▪ The contentious **interest cap law** continues to erode the rich margin between loan and deposit rates with significant decline in credit growth to the private sector.
	Deteriorating asset quality	▪ **Slower private consumption growth, layoffs and delayed government payments** has affected **asset quality** in trade, communication & transport, personal & households and real estate

Corporate Governance

In April 2018, 'The Code of Corporate Governance Practices for Issuers of Securities to the Public 2015' by the Capital Markets Authority (CMA) came into full effect. This code advocates for the adoption of standards that go beyond the minimum standards prescribed by legislation. As a board, this remains our core guiding principle as we continue to exercise our mandate of protecting stakeholder interests and enhancing investor confidence in the Bank.

In 2018, the notable change in the composition of the Family Bank Board of Directors was the exit of Dr. David Thuku following his retirement as the Managing Director and Chief Executive Officer of the Bank, in November 2018. On behalf of the Board of Directors and staff, I sincerely express the Bank's appreciation to Dr. Thuku for his contribution to the Bank. Dr. Thuku steered the bank through a turbulent season for the banking sector, following the introduction of the interest-rate capping. He left the Bank having pulled it back to profitability. We wish him well in his future plans.

Future Outlook

Across the sector, strategy has predominantly focused on rationalizing structure and streamlining operations. The sector is now turning to digitization, new technology and data governance, among others. At Family Bank, we are a step ahead and are now expanding the innovation to borderless banking.

At the centre of any trading activity is money and the efficient settlement of trade obligations. Traders can attest to the importance of a secure, fast, convenient, and affordable means to remit funds across borders instantly and promote international trade. We are leading in this innovation through our service dubbed Family Bank Remit that is available to both customers and non-customers and enables users to send money easily and conveniently to more than 10 destinations in Africa and beyond through our mobile application PesaPap. This facilitation for trade and settlements is expected to contribute greatly to the growth of Small and Medium Enterprises (SMEs) in Kenya

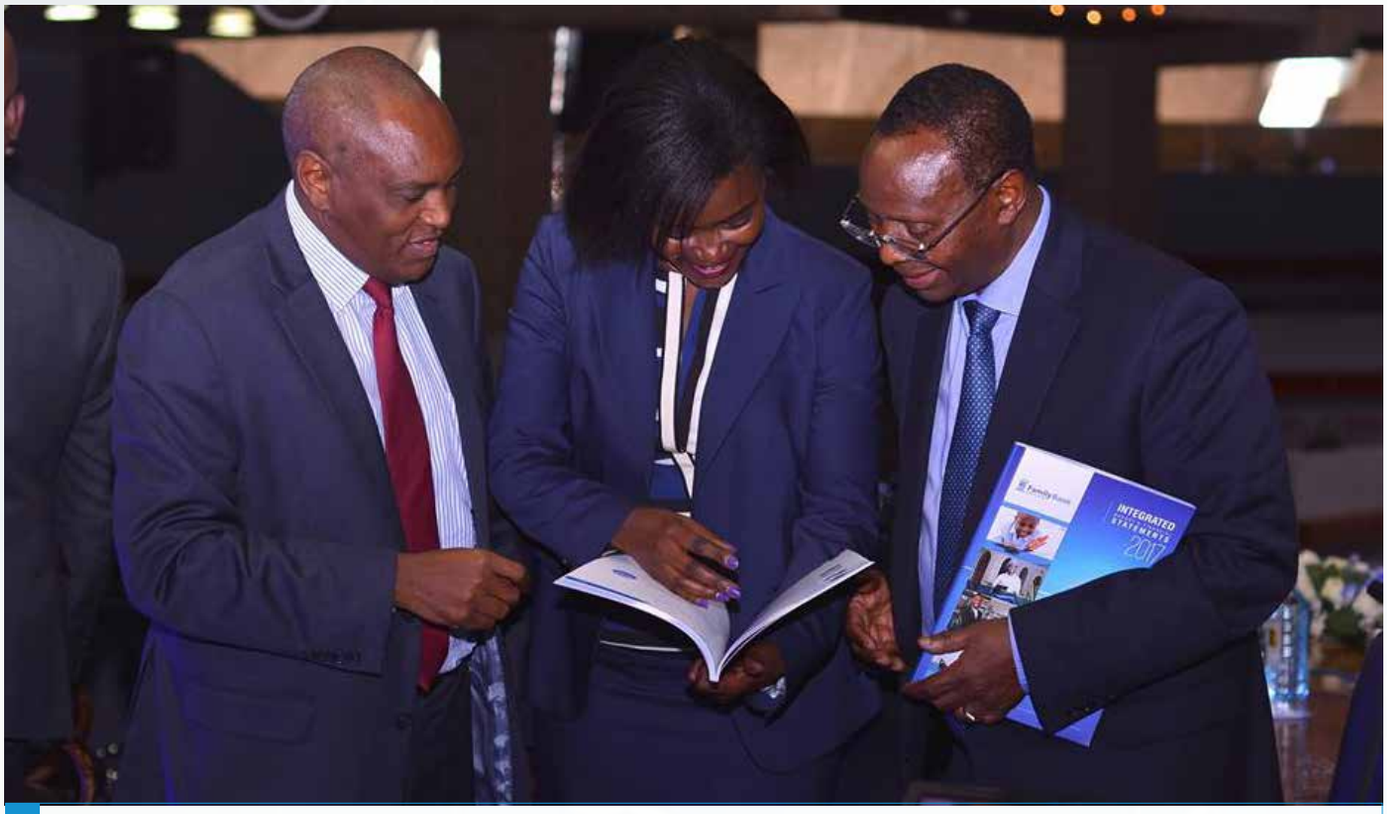
As a bank we also recognize the ever-growing need for business capital as well as operations and growth financing within the SME sector. We shall actively continue to lend to this sector and support local entrepreneurs to build sustainable SMEs and create more employment opportunities for the Kenyan youth. It is estimated that the SME sector employs about 87% of youth in Kenya.

Finally, our operating environment demands total compliance with the regulations and guidelines on AML and KYC. We are committed to maintaining a high level of vigilance to ensure strict compliance with all guidelines and the rule of law.

Chief Executive Officer Designate

On behalf of the Board, we are delighted to formally introduce Ms. Rebecca Mbithi as the Chief Executive Officer Designate of Family Bank Ltd, subject to approval by the Central Bank of Kenya. Rebecca is the current Company Secretary and Director, Legal Services - a position she has held with the Bank for the last 4 years. Rebecca is a highly experienced professional with an extensive background in leadership in various organizations at director level specializing in law, project finance, Corporate Restructuring, Equity/ Debt raising and Governance. She holds a Bachelor of Laws (LLB) degree from the University of Nairobi and a Masters in Business Administration from the United States International University. She is a Certified Public Secretary and a Certified Public Accountant of Kenya.

At Family Bank, she has been instrumental in Strategy and Business Development, Capital and Debt Raising, Risk Management, Compliance and Controls, providing legal services and strengthening the Bank's Governance structures. We are confident that Ms. Mbithi has what it takes to steer this great Bank to the next level.



Family Bank former MD & CEO Dr. David Thuku, Family Bank Company Secretary & CEO Designate Rebecca Mbithi and Dr. Wilfred D. Kiboro, Family Bank Board Chairman during last year's AGM.

Conclusion

We are optimistic about the prospects for the banking industry even as discussions on lifting the interest rate cap continue. In the same breath, we are optimistic about Family Bank's growth prospects in 2019, having implemented strategies and measures that have already set us on a strong growth path. Our focus as a business going forward is to grow our revenue base while capitalizing on the exponential growth in mobile banking.

I am confident in our staff and the management team. I believe that Family Bank is poised for inordinate success.

Thank you.

Dr. Wilfred D. Kiboro
Chairman- Board of Directors

STATEMENT FROM THE Ag. MD & CEO

Dear Shareholders,

The year 2018 marked a new chapter for the Kenyan banking industry for many reasons. One of those reasons is the full implementation of the International Financial Reporting Standards version nine (IFRS 9 - financial instruments). This new standard of accounting replaced the International Accounting Standards (IAS 39) and it covers classification and measurements of financial assets; Impairment of provisioning for loans and advances, and classification & measurement of financial liabilities. This implementation was expected to impact provisioning, the most significant change being the move from the incurred to the expected credit loss model for impairment of financial assets. As a testament of its resilience, the industry went against expectations to record significant growth.

At Family Bank, we recorded a remarkable turnaround to record profits with a consistent growth throughout the year. This upward trajectory was made possible by increased focus on costs containment, accelerating penetration of digital banking services and growing the bank's non-funded income lines.

As a Bank, we are focused on positive growth and creating value to all our esteemed stakeholders. I wish to extend my sincere appreciation to the Board of Directors, our ever-loyal customers, and the Family Bank fraternity across the 91 branches, for without them, we would not have had a remarkable turnaround.

Financial Performance

We shrugged off a tough operating environment and a sluggish economy to report a Profit Before Tax of KES 435 Million for the Financial Year ended December 2018, reversing a KES 1.36 Billion loss the previous year.

We registered a KES 1.35 Billion reduction in operating costs, translating to a 19% saving relative to the 2017 financial year. Our deposits grew by 2.4% to hit KES 48.5 Billion while the loan book remained largely steady, recording a growth of 1.5% to KES 44.1 Billion. The quality of the loan book improved in the 2018 financial year where we posted a 17% reduction in loan loss provisions to KES 771.9 Million. This was after a decline in non-performing loans by KES 1.23 Billion to KES 7.1 Billion during the year. Non-interest income grew by 15% from the previous year while staff costs reduced by KES 480 Million from KES 2.34 Billion in 2017 to KES 1.86 Billion.

Adoption of Digital Channels

We are firmly on the digital transformation journey which is designed to improve service delivery across all our touch points and provide value to our customers. This has seen over 70% of our transactions migrate to our digital channels and this number continues to grow.

2018 was a great year that saw the Bank premier innovations within the FinTech space. The Bank heavily invested in the revamp of our mobile banking platform, PesaPap, specifically to improve the user and navigational experience and introduce instant mobile loans. Since the launch of the mobile application in July 2018, we have advanced over KES 755 Million.

Left - Family Bank former MD & CEO Dr. David Thuku, Kenya Bankers CEO Dr. Habil Olaka, Family Bank Head of Strategic Partnerships Nancy Njau and Chief Operations Officer Godfrey Kamau go through the revamped PesaPap App at the launch of revamped PesaPap mobile banking platform. Right - Family Bank Management at the launch of the revamped PesaPap.

Family Bank also scored another first to offer an instant money transfer service from Kenya to China via WeChat- China's largest messaging, social media and mobile payment App – in partnership with London-based financial technology firm SimbaPay. WeChat integration will be a game changer for thousands of local businesses that trade with their business counterparts in China. The service dubbed Family Bank Remit is available to both customers and non-customers and enables users to send money easily and conveniently to other destinations in Africa and India through our mobile application PesaPap.

Family Bank Chief Operations Officer, Godfrey Kamau explaining to the Chairman Kenya National Chamber of Commerce and Industry, James Mureu at the Chinese Home Expo in Nairobi where Family Bank got an opportunity to showcase Family Bank Remit, an instant money remittance solution.

Senior Officials from the Chinese Embassy in Kenya and the Kenya National Chamber of Commerce and Industry at the Family Remit Stand at the China Home Expo in December 2018.

In 2018 we expanded our merchant acquiring business by introducing merchant point of sales devices to support card business. Further, we revamped our Internet Banking Platform enhancing user experience, functionality and improving the look and feel. The Bank also partnered with Telkom Kenya to offer their mobile money services on our mobile banking platform and in our branches. Plans are underway to extend this service further through a shared agency network.

Branch Rationalization

The migration of transactions to our digital financial services has reduced traffic to our Branches. This made us relook at our branch footprint with a view to optimising our physical presence and resource allocation. With this regard, the Bank sought approval from the regulator, the Central Bank of Kenya, to rationalize and consolidate our branch network. Family Bank Tom Mboya branch in Nairobi relocated to River Road West on River Road, a growing hub in the lower part of Nairobi's Central Business District. We also moved operations of our Bamburi branch to Digo branch and Kisumu Reliance branch to Kisumu Express branch.

Products and Services Support

- **Shop and Win Visa Card Promotion** – In a bid to drive usage of our Family Bank Visa Debit Cards, we rewarded our customers through a consumer promotion dubbed Shop and Win over an 8-week period, which saw customers from across our branch network bag cash prizes.

Shop & Win: Jovial faces as Pricila Alivitsa, a farmer and customer from Kakamega County is awarded KES 100,000 during the Shop & Win Visa Card Promotion by Dr. David Thuku (left) Family Bank former MD and the Chief Operations Officer Godfrey Kamau.

- **Trade Finance Exhibition** – Family Bank is in the fore-front of empowering our customers' businesses and to this end the Bank co-sponsored a Trade Finance workshop, an event that provided a platform for empowering importers and equip them with valuable information on importation procedures and financing options.
  The Bank has established a Trade Centre in Mombasa as a strategy to serve this key market for trade finance services. We have began to see the growth in revenues from this segment.

- **Family Bank Business Club** – Family Bank Business Club continues to provide an invaluable networking platform to our customers. In 2018, the Business Club held a number of business seminars and its annual business exposure trips.

Outlook for 2019

As we embark on the 2019 journey, I believe that our business can only get better. We have a solid strategy in place to deliver an exceptional 2019. We have a rich talent pool in the Bank and with the unwavering support from our valued shareholders and customers, we can only be the best. We have prioritized the following focus areas:

1. Attaining Customer Experience Excellence - We aim to attain excellence not only in our internal operations but also in our interaction with customers across all touch-points. We recognize that keeping our customers at the center of what we do, is crucial to building advocacy and as a consequence, attracting new and incremental business. Attaining Customer experience excellence will require addressing our turnaround time on customer instructions and complaints, ensuring maximum availability of our systems and optimizing on the functionality of our digital platforms.

   In order to ensure that we continuously improve on customer experience, we shall undertake targeted research to measure our customer advocacy scores, as well as to obtain feedback on the things that are working well and those that require improvement. We shall also continue to have direct engagements with our customers through branch and regional customer forums.

2. Re-invigorating our Brand – Having gone through a difficult period over the last two financial years, the brand suffered a setback. This is now part of our history. In 2019, we have set out to rebuild and re-invigorate the Family Bank brand to be the household brand we have always envisioned it to be. We shall continue engaging our stakeholders through on-ground, online, print and electronic platforms to build top-of-mind awareness of our brand and our competitive bouquet of products and services.

3. Accelerating Innovation – Family Bank has for long been known for being the industry leader in innovation. Maintaining this leader status is our imperative. Digital innovation indeed ranks top amongst the enablers to customer experience excellence that we have outlined above. We shall therefore continue with the aggressive digitization of our banking processes, adoption of transformative technology and creation of new value adding digital services, in line with the needs of our customers.

4. Value chain solutions – As part of our product innovation strategy, we are also targeting solutions that increase productivity and promote collaboration between enterprises within select high potential value chains. We believe that this will deepen the integration of SMEs and build shared prosperity through access to new markets, improving their distribution processes and building SME brands.

Conclusion

Our brand has what it takes to propel itself to the next level. With a shared value and culture system harnessed by the synergy of various arms of the Bank, I am confident that the best is yet to come.

Thank you to our shareholders, customers, the Board, management, staff, and various strategic partners for walking this journey with us. Our vision remains to be the financial institution that leads to the positive transformation of people's lives in Africa.

Thank you and God bless you.

Charles Njuguna
Ag. MD & Chief Executive Officer


pesa pap!
Sasa
ku-save na
ku-access
loan ni rahisi!
Pesa Bila Stress!
Get instant loans
with PesaPap Mobile Banking!
Download PesaPap App or Dial *325#
Family Bank
With you, for life
+254 (020) 3252 000/ +254 703 095 000
+254 (020) 3252 445/ +254 703 095 445
customerservice@familybank.co.ke
www.familybank.co.ke
www.facebook.com/familybankkenya
www.twitter.com/familybankkenya
Family Bank is regulated by the Central Bank of Kenya

Sustainability Review 2018

SUSTAINABILITY REVIEW

Contents

ABOUT THIS REPORT

We are pleased to present our second Sustainability Report for the year ended 31st December 2018, following our inaugural report covering 2017. This edition gives a detailed overview of the Bank's sustainable business efforts, commitments and achievements in the year under review.

The banking industry is a key driver for the economic growth of our country. Banking enables businesses to thrive, create jobs and change lives of people and communities right from grassroots to across borders.

As a key player within the industry, Family Bank's sustainability agenda revolves around three key pillars:

- Building a sustainable banking business
- Contributing positively to Kenya's economy
- Investing in the community in which we conduct our business

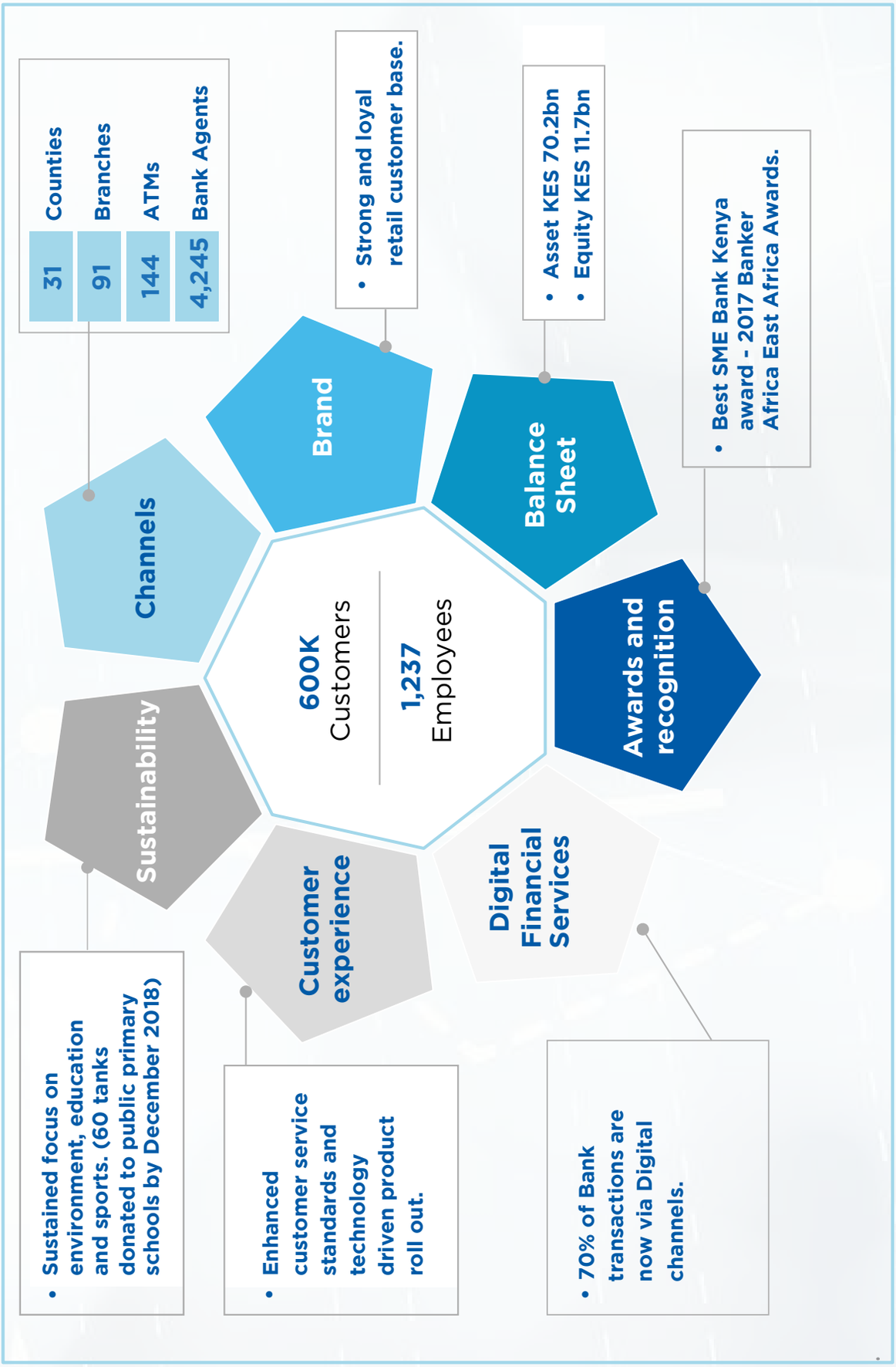
Building a sustainable banking business in line with the UN Sustainable Development Goals (SDGs) and the UNEP Finance Initiative - Principles for Responsible Banking 2018 which drive ambition and challenge banks to continuously increase their contribution towards a sustainable future, creating value for both society and shareholders, and help banks build trust with investors, customers, employees and society. We are keen on delivering on our brand promise of 'with you for life' embedded in our core values centered around transparency, humility, winning together and self-belief; to build a firm fit for the 21st Century.

Contributing positively to the Kenya's economy is our corporate call to national duty and we are keen to honour and fulfil this promise to our motherland. Empowering the community in which we conduct our business is the pride of our family.

We strive to empower families, the core unit of any society, through sustainable community investment programs that resonate with our customers. Our community investment programs are concentrated on four key areas:

- Education
- Nurturing sports talent
- Water and Sanitation
- Afforestation to combat climate change

FAMILY BANK AT A GLANCE



OUR STAKEHOLDERS

At Family Bank, we acknowledge that a credible corporate responsibility approach must include ongoing relations with primary stakeholders. We identify our primary stakeholders as those whom we impact during our operations or have an impact on our ability to operate. These stakeholders are: customers, investors/shareholders, regulators and government, employees, society, and suppliers.

The sustainability agenda of our business is driven by the needs of our stakeholders.

1. Investors
2. Employees
3. Customers
4. Regulators & Government
5. Communities
6. Media
7. Suppliers

We continue to create value for our stakeholders driven by our mission of positively transforming people's lives by providing quality financial services through innovative, efficient and reputable practices to impact and drive value to the society and the wider macroeconomic environment. To achieve these sustainability considerations (social, economic and environmental) and in order to enrich relations with the above stakeholders, the Bank has reviewed its engagement process to offer a variety of ways for stakeholders to contact us and inform us of their needs and concerns in real-time. We are actively maintaining various channels of communication, learning what we are doing well and where to improve in our day to day activities.

The table below looks at each stakeholder as per the parameters defined above.

Stakeholder	Description	Key Concerns	Value Delivered
Shareholders	They are initial providers of core financial capital and we disclose to them relevant information to make informed investment decisions as well as seek their perspectives on our financial performance and Strategy.	The key concerns raised by shareholders related to credit risks considering the introduction of interest rate capping and IFRS 9. They were also concerned about business growth prospects in a challenging operating environment. A greater number of shareholders showed interest in how we are embedding sustainability considerations into our business practices.	• Increased net asset value and earnings per share. • Continuous engagement to ensure full disclosure and open communication to inform their investment decisions.
Customers	Customers remain the largest source of our deposits (financial capital), which enable us fund lending activities. More customers mean greater revenue growth and this can only be achieved by providing superior customer experience. On the other hand, sustainable banking practices and world-class governance and risk management ensure we maintain the trust customers have in us.	They desire banking to become simpler, more intuitive and time-efficient. Excellent customer service, getting it right for customers first time and security for their money and data.	• Secure deposits, investments and wealth, while growing returns. • Sustainable credit that enables wealth creation, economic development and job creation. • Multiple banking channels. • Financial inclusion through affordable products to the previously unbanked. • Innovative solutions that meet their needs.
Employees	Staff are our greatest asset and key stakeholder. They are the face of the business. We are cognizant of the contribution of our	They want to grow as the business grows, open doors for career progression, opportunities to contribute to society and a work environment that	• Employment • Performance-based promotions • Local and International Training

Stakeholder	Description	Key Concerns	Value Delivered
	staff in building this brand and delivering value to our stakeholders.	is friendly, safe and conducive for work life balance.	• Employment equity and gender equality • Continuous improvement of processes.
Society	We know that our business cannot succeed in a failing society. Society grants us the decisive license to operate. Our vision as a Bank is to positively transform the lives of people in areas we operate.	Banks greater influence on their customers and employees to prioritize environmental, social and governance matters.	• Transform people's lives through sports, water, education and health. • Sustainable banking practices and regulatory compliance.
Regulators & Government	Good Corporate citizenship is non-negotiable to us through implementation and compliance with public policies.	Regulation for the banking industry continues to be around key areas such as cyber security, business and professional conduct, corporate governance, financial reporting and financial crime.	• Taxes • Compliance with laws and regulations • Purchase of government and public-sector bonds
Suppliers	The extensive network of suppliers is not only vital to our ability to provide high-quality financial services reliably and efficiently, it also represents an opportunity to extend our ability to positively impact the communities and environments in which we operate.	Supplier diversity	• Procurement program that caters for special interest groups: women, youth etc.

We want them to provide input as the Bank builds its understanding of how its activities might positively or negatively impact key socio-ecological thresholds.

MATERIAL MATTERS

Family Bank Material Issues and Sustainable Development Goals (SDGs)

In 2015, world leaders promulgated the Sustainable Development Goals (SDGs) after the Millennium Development Goals (MDGs) period ended. SDGs define global sustainable development priorities and aspirations for 2030 and seek to mobilize global efforts around a common set of goals and targets. The SDGs call for worldwide action among governments, business and civil society to end poverty and create a life of dignity and opportunity for all, within the boundaries of the planet.

The SDGs present an opportunity for business-led solutions and technologies to be developed and implemented to address the world's biggest sustainable development challenges. As the SDGs form the global agenda for the development of our societies, they will allow leading companies to demonstrate how their business helps to advance sustainable development, both by minimizing negative impacts and maximizing positive impacts on people and the planet.

Family Bank is in the processing aligning its strategy to the SDGs to augment its mission of positively transforming people's lives by providing quality financial services through innovative, efficient and reputable practices. The Bank's material issues are aligned to the 2030 Agenda (SDGs) as below:

Financial Inclusion	1 NO POVERTY
Talent Management and Diversity	5 GENDER EQUALITY; 8 DECENT WORK AND ECONOMIC GROWTH; 10 REDUCED INEQUALITIES
Ethics and Integrity Customer privacy	11 SUSTAINABLE CITIES AND COMMUNITIES; 16 PEACE AND JUSTICE STRONG INSTITUTIONS
Empowering Communities	3 GOOD HEALTH AND WELL-BEING; 4 QUALITY EDUCATION; 6 CLEAN WATER AND SANITATION
Environmental Footprint Sustainable financing	11 SUSTAINABLE CITIES AND COMMUNITIES; 13 CLIMATE ACTION
Product Development and Digital Innovation Customer satisfaction and communication	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE

1. Financial Inclusion
2. Talent Management and Diversity
3. Ethics and Integrity
4. Empowering Communities
5. Environmental Footprint
6. Product Development and Digital Innovation
7. Customer Privacy, Satisfaction and Communication
8. Sustainable Financing

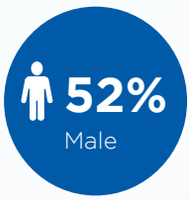
1. Financial Inclusion

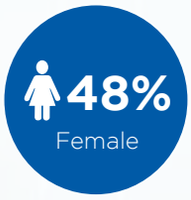
Financial Inclusion today is a stated goal for both private and public sector actors. Among international organizations, Financial Inclusion is mentioned in the Sustainable Development Goals (SDGs). We have deployed advanced technology to provide access to payments and savings, protect against crises and mobilize resources essential for investment and consumption.

	2017	2018
Number of Family PesaPap Agent outlets	4,007	4,245
Registered PesaPap mobile banking customers	599,000	633,784
Number of PesaPap Wallet loans processed	1,018	73,106
Value of PesaPap Wallet loans processed (KES)	24,799,740	755,044,860

2. Talent Management and Diversity

The Bank has employed a total of 1,205 employees, 52% male and 48% female. 504 employees are below 30 year. 638 employees are between 31-40 years. 89 employees are above 41 years and only 6 are above 51 years. The Board of Directors comprises of seven (7) directors of which two (2) are female. The Banks senior management comprises of eight (8) staff of which two (2) are female. Remuneration is based on performance except for new hires whose salary depends on their entry grade. Annual Director Fees is KES 1,600,000 (KES 400,000 per quarter).





The Bank runs a comprehensive training scheme with three (3) days as the average number of training days per employee.

Further, Occupational Safety and Health Audits (OSHA) are conducted annually at all facilities and reports filed with relevant authorities. Recommendations are acted on through a continuous improvement process.

3. Ethics and Integrity

The Board of Directors and Management of the Bank have put in place stringent policies and structures to ensure good corporate governance and strict adherence to the rule of law as it undertakes its business and mandate to its customers, regulator and shareholders. The Bank has invested in a robust Anti-Money Laundering system with the ability to detect suspicious transactions, put in place measures to ensure strict compliance with our Know-Your-Customer (KYC) policy, introduced regular mandatory training for all serving staff and rolled-out a detailed induction curriculum for all new hires.

Fraud - The Bank experienced 169 fraud cases in the reporting period of which 49 were successful and 120 unsuccessful. The number of employees dismissed as a result of fraud was 28.

Whistleblowing portal – The whistleblowing portal seeks to inculcate a 'speaking up' culture among employees and provides a mechanism for giving feedback or reporting non-compliance or corruption cases anonymously, securely and confidentially. Employees need a trusted reporting process to raise issues involving improper, unethical or inappropriate behavior, and this portal relays such concerns for review, investigation and action. All these efforts are targeted towards improving ethics and integrity at the Bank.

4. Empowering Communities

Our vision is to be the financial institution that leads in the positive transformation of people's lives in the region because we know that we are as strong as the communities we operate in. Our brand promise to our customers 'With you for Life' goes beyond our provision of financial services to improving the lives of the people in the communities in which we operate through 4 key pillars: Education, nurturing sports talent, Water and Sanitation and afforestation to combat climate change.

Education

Inclusive and equitable quality education is one of the Sustainable Development Goals by the United Nations that seeks to promote lifelong learning opportunities to all. One of the defining factors of our focus on the education pillar is to increase access to secondary schooling by providing comprehensive scholarships and holistic growth of the students through The Family Group Foundation.

- Scholarship Programmes

  A total of 474 students have been offered scholarships both in high school and tertiary. As at December 2018, the Foundation had 296 students under its scholarship programme. 102 students in the sponsorship programme sat for their Kenya Certificate for Secondary School Education (KCSE).

Family Bank Company Secretary Rebecca Mbithi with the top KCSE 2018 student under the Family Group Foundation Scholarship programme.

- Mentorship Programmes

  Over the years the Bank has been running a mentorship programme for students through the Family Group Foundation. This program targets students under the Family Group Foundation scholarship fund. In 2018, all sponsored students had a three-day workshop where they were taken through counselling on academic, personal and career-related aspects of their lives. All beneficiaries are paired with mentors from the Foundation's benefactors who come from all Family Bank branches across the country. The 2018 Mentorship Programme attracted the CEOs of Family Bank and Kenya Orient Insurance Company who interacted and talked to the sponsored students.

• Afya Elimu

In 2015 we partnered with the Higher Education Loans Board (HELB) and other partners to roll out the Afya Elimu Fund. The Afya Elimu Fund aims to support over 2,500 health workers during the first year and a further 1,500 health workers every year in the fields of nursing, clinical medicine, laborato-ry services, nutrition and health records information technology.

This partnership will see us donate KES 10 Million through the Family Group Foundation. The support from the Family Group Foundation will be sufficient to educate at least 100 students over this period. This will be a significant contribution towards reducing the shortage of health workers across the country. To date the Foundation has contributed KES 4 Million that has supported 42 students at the Kenya Medical Training College. In 2018 we donated KES 1.25Million towards this programme.

Sports

The Family Bank Eldoret Half Marathon was launched in 2007 as a platform to nurture raw talent in an already fertile ground for champions in Eldoret, Uasin Gishu County and the surrounding counties. 2018 marked the 12th edition and rebrand of the Half-Marathon to Family Group Eldoret Half-Marathon to incorporate other entities with whom the Bank shares a common shareholding. The same year also saw the entrenchment of our cause for inclusive education for children living with autism. Under the rallying call 'Champions run for Autism' we aim to build more centres to cater for children living with autism and improve on the 97 centres existing in the nation.

Champions run for Autism

Water and Sanitation

• Supporting Water, Sanitation and hygiene

In 2018 Family Bank partnered with water.org, an international Non-Governmental Organization whose key area of focus is the improvement of water and sanitation access and standards globally. This partnership will see the Bank offer loan facilities to water, sanitation and hygiene (WASH) service providers and at the same time attain the social impact goal of achievement of the Sustainable Development Goal (SDG) 6 that focuses on ensuring access to clean water and sanitation for all.

• Maji Kwa Wanafunzi

In 2018 Maji Kwa Wanafunzi , the Staff CSR Initiative, saw the Bank donate 25 water tanks to various public primary schools across the country. Through this worthy initiative, Family Bank members of staff from the 92 branch network and the Head Office Departments passionately contribute to the improvement of public sanitation. Since its launch in 2017, this staff CSR initiative has seen the Bank donate over 60 water tanks to various public schools across the country, impacting over 40,000 students. The initiative is aimed at transforming the lives of school going children through provision of clean drinking water.

This hugely succesful project, in which the Bank matches all staff contributions shilling-for-shilling had targetted to impact 40,000 learners countrywide over a three year period. We have already attained this target.

Family Bank Staff from various branches and departments present water tanks donated to various schools through the Maji kwa Wanafunzi staff CSR initiative.

Other Partnerships

Partnerships, in core areas such as education, community empowerment and health, are a key strategic focus for the Bank.

- Mount Kenya University

  In 2017, we partnered with Mount Kenya University to offer mentorship to young entrepreneurs, who are graduates of the university's Graduates Enterprise Academy (GEA). The mentorship, which is orchestrated through our Business Club, offered free mentorship sessions on best business practices, business funding and growth.

- Junior Achievement Kenya

  The Bank has an annual partnership with Junior Achievement Kenya (through the Kenya Bankers Association) that gives opportunities to high school students to visit corporates for a job shadow programme. This programme accords students an opportunity to gain hands on experience and exposure at the work place. This not only provides the bank with an opportunity for mentorship but also provides a platform for exposure to students to enable them make informed career decisions at an early stage. We are happy to support such initiatives that mould careers of the youth.

- Partners in Action for Community & Environment (PACE)

  The Foundation also organised community service programmes that sought to foster community spirit and a sense of patriotism for the form four leavers. High school graduates from the scholarship program were assigned to different schools to work as teaching assistants in providing learning support in under-resourced schools. The project in 2017 was a pilot project in the partnership between PACE and the Foundation. It started off with seven volunteers who are alumni of the Family Group Foundation sponsorship programme. This year the Foundation plans to absorb more of its alumni into the community program.

5. Environmental Footprint and Afforestation

In 2018, the Bank partnered with the Nation Media Group to drive a countrywide tree planting initiative that will see both corporates plant over 15 Million trees over the next five years. This is in line with the governments agenda of planting 1.8 Billion trees by 2022. Since launch of this initiative dubbed Trees for Life, the Bank has held tree planting exercises in Machakos, Kiambu and Nairobi counties.

Left - Family Bank Board of Directors at the launch of Panda Miti, Penda Kenya tree planting initiative officiated by the President, H.E Uhuru Kenyatta in June 2018
Right - The Launch of Trees for Life tree planting initiative at Kyemutheke Youth Vocational Training Centre in Machakos County.

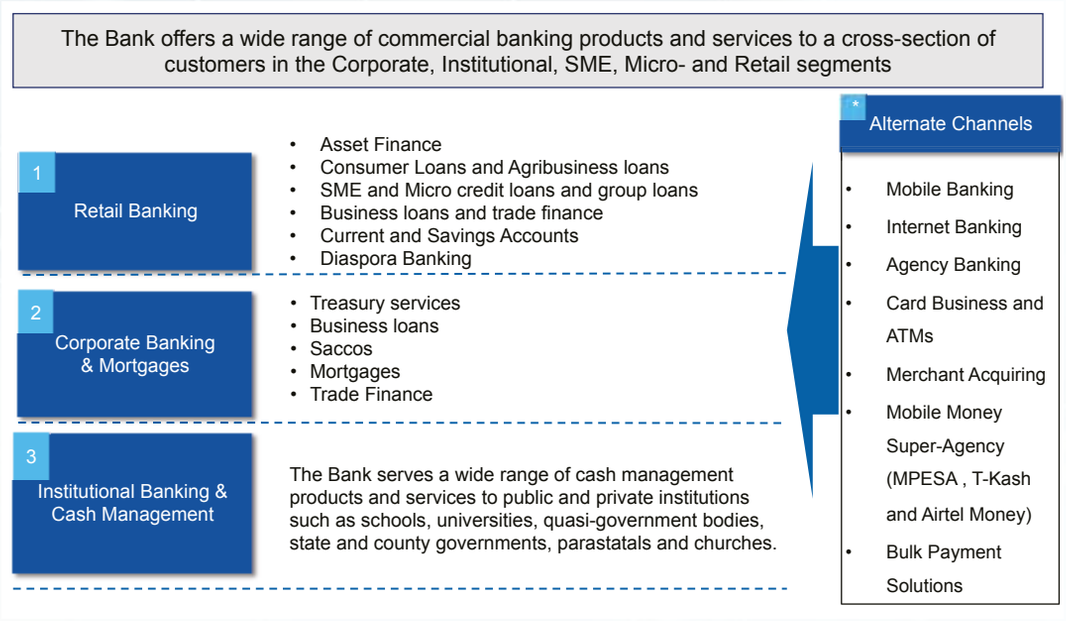
6.Product Development and Digital Innovation

In 2018, the Bank launched two (2) new product offerings and improved one (1) process:

- Revamped PesaPap- The mobile industry has played a great role in aiding financial inclusion in the banking sector. In July 2018 the Bank launched a revamped PesaPap Application which has seen both customers and non-customers access instant mobile loans, set investment goals through the incredible user interface at the click of a button.

- Family Bank Remit – The Bank partnered with London-based financial technology firm SimbaPay to launch an instant money transfer service from Kenya to China through WeChat in November 2018. With over 1 billion subscribers, WeChat is the largest payment and social media app in China. This initiative connects Africa's largest mobile money ecosystem to China's largest payment service in real-time. This service is helping boost Kenya-China trade.

- Self-registration of PesaPap Mobile Banking – to improve service delivery to our mobile banking customers, the Bank introduced a self-registration option for PesaPap. Customers can now register and activate PesaPap without the need to visit any physical bank branch or fill out forms. PesaPap can be accessed by dialing USSD code *325# or by downloading the PesaPap app available on Google Play Store and Apple Store.



7. Customer Privacy, Satisfaction, and Communication

Family Bank respects customer privacy and are committed to keeping their personal information and other data confidential and secure. All employees are continuously trained in ways to ensure zero breaches of customer data especially during induction.

We do not otherwise disclose customer data information to third parties unless with their express permission and instructions or we are under a legal or similar obligation, for example from regulators or a court of law.

The Bank has a call centre with a dedicated team of 25 agents available to respond to customers queries 24 hours a day, 7 days in a week. We also have an online chat facility available on the Bank's website. We have deepened our customer interations through social media (Facebook, Twitter, LinkedIn, and WhatsApp).

Social media numbers as at 31st December 2018:

- Facebook- **43,261**
- Twitter - **16,086**
- LinkedIn – **15,572**

8. Sustainable Financing

Family Bank has been instrumental in supporting agriculture, trade, tourism, transport and construction which are key measures of Kenya's economic growth. Further, our retail banking business and lending to individuals also indirectly supports the aforementioned sectors.

Our impact in the various sectors over the years has continued to rise, and below is an analysis of the Bank's support.

Agriculture

Agriculture is the single biggest contributor to Kenya's GDP accounting for 31.5% of the total in 2017, according to the Kenya National Bureau of Statistics (KNBS). Sustainable agriculture and food security has been identified as a key deliverable for the sitting Government of Kenya, forming one of the pillars in the 'Big 4 Agenda', mainly focusing on increased production, productivity and value addition. Family Bank traces its origin from this sector having been founded to especially support farmers in the tea sub-sector in Central, Western and parts of the Rift Valley.

In 2018, our lending to agribusiness stood at KES 2.28 Billion forming a substantial contribution to our loan portfolio. Family Bank is proud to contribute to this sector.

Trade

The trade sector in Kenya is diverse but mainly driven by retail trade. This category also includes the hospitality industry which is the linchpin of the country's tourism sector. Notably, this sector accounts for majority of Small and Medium Enterprises (SMEs) in Kenya which in turn form a significant driver of economic growth and job creation.

The Trade Sector is a key driver of our business, forming the single largest component of our loan book at KES 18 Billion in 2018.

Manufacturing

The Big 4 Agenda by the Government of Kenya prioritizes manufacturing as one of the pillars for economic growth. Family Bank continues to support the growth of this sector through lending and offering banking services to SMEs in manufacturing and light industries.

Our lending to the manufacturing sector stood at KES 270 Million in 2018 compared to KES 155 Million in 2017, which is close to double growth in value.

Real Estate and Construction

The construction and real estate sector has seen rapid growth mainly driven by Kenya's expanding population and rapid urbanization. In light of this, affordable housing is one of the 'Big 4 Agenda' deliverables as set out by the Government of Kenya. In 2018, we lent a total of KES 12 Billion to the real estate and construction sectors.

CORPORATE GOVERNANCE STATEMENT

1. STATEMENT OF COMPLIANCE

The Board and management of the Bank continue to comply with the Code of Corporate Governance Practices for Issuers of Securities to the Public 2015 and Corporate Governance guideline prescribed by Central Bank of Kenya (CBK) in the Prudential Guidelines for the banking industry. The Board recognises the fundamental role of corporate governance in enhancing the culture and business performance and that high standards of corporate governance are a key contributor to the long term success of a company, creating trust and engagement between the company and its stakeholders.

The Group (Family Bank Limited and its subsidiary, Family Bank Insurance Agency Limited together referred to as the 'Group') has adequate policies and procedures in place that are reviewed regularly and which include:

- Clearly defined responsibilities and authority of directors, the Managing Director and management;
- Established corporate objectives and strategies;
- Recognition of the interests of various stakeholders;
- Alignment of corporate activities and behaviour in compliance with applicable laws and regulations; and
- Protection of the interests of depositors and other creditors.

The Board in December 2015 updated its Board Charter so as to bring in it line with the key values of the Bank, generally accepted Principles of Good Corporate Governance and in compliance with the sound corporate governance principles under the Prudential Guidelines published by the Central Bank of Kenya as well as the Companies Act 2015. The purpose of the Board Charter is to provide:

- The demarcation of the roles and responsibilities, functions and powers of the Board and management.
- The relevant principles of the company's limits and delegation of authority and matters reserved for the Board.
- The policies and practices of the Board in respect of matters such as corporate governance, conflict of interest, board meetings, composition of the Board, appointment, induction and evaluation.

2. RELATIONS WITH SHAREHOLDERS

The Board recognises the importance of good communications with all shareholders. The Annual General Meeting (AGM) as well as the published annual report is used as an opportunity to communicate with all shareholders. The Company always gives shareholders the 21 days' notice of the AGM as provided for in the Kenyan Companies Act and shareholders are encouraged to submit questions and also appoint proxies to represent them where they are unable to attend. Ad hoc shareholder requests for information are handled on an on-going basis and also on the floor of the AGM. The Board uses electronic means to communicate with shareholders and shareholders are encouraged to visit the website familybank.co.ke and click on investor relations for general information on the Company as well as annual reports. In upholding and protecting shareholders' rights, the Board recognises that every shareholder has a right to participate and vote at the general shareholders meeting. The Board also invites shareholders to seek clarity on the Bank's performance in general meetings.

3. BOARD COMPOSITION

The Group has a competent Board of Directors bringing together diverse backgrounds and expertise necessary to provide leadership to the Bank.

Principle on Structure of the Board

To ensure effectiveness and value addition, Family Bank Board of Directors are highly qualified in varied fields, which is essential in enabling them to:

- Have proper understanding of, and competence to deal with, the current and emerging issues of the business;
- Exercise independent judgment;
- Encourage enhanced performance of the Group;
- Fairly reflect the Group's shareholding structure; and
- effectively review and challenge the performance of Management.

CORPORATE GOVERNANCE STATEMENT (Continued)

4. BOARD INDEPENDENCE AND CONFLICT OF INTEREST

The Prudential Guideline No 2 prescribes the criteria for independence and minimum ratio of independent directors to the total Board of Directors as one- third. The Bank is in compliance with these requirements. The Board has set standards to ensure the Directors' independence. The fundamental premise of the standards is that any Director is independent of management and free of any business or other relationship that could materially interfere with exercising their independent judgement. The Directors are required to disclose their areas of conflict. Directors are required to refrain from contributing to or voting on matters in which they have such conflict.

As a Board we encourage independence by objectively challenging management; challenging each other's assumptions, debating constructively and deciding dispassionately. Our decisions are aimed at supporting the ultimate good of the organisation. The Chairman ensures that Board decisions are taken on a sound and well-informed basis while encouraging critical discussion to ensure that dissenting views can be expressed and discussed within the decision-making process, all the while upholding the principle of collective responsibility for Board decisions.

The role of Chairman and the Managing Director are separate and distinct. The Board maintains a good working relationship with the Managing Director, Executive Directors and management without detracting from the Governance Principles of Accountability and Independence that must exist to ensure sustainable performance.

The Chairperson

The Chairperson of the Board is an Independent Non-Executive Director. The Chairperson leads and manages the work of the Board and ensures that decisions are taken on a sound and well-informed basis. The Chairperson provides leadership to the Board and is responsible for the Board's effective overall functioning.

The Chairperson also ensures:

a) The smooth functioning of the Board, the governance structure and instils a positive culture in the Board;
b) Guidelines and procedures are in place to govern the Board's operation and conduct;
c) All relevant issues are on the agenda for Board meetings and all Directors are able to participate fully in the Board's activities;
d) The Board debates strategic and critical issues; and
e) The Board receives the necessary information on a timely basis from management.

The Chief Executive Officer

The Chief Executive Officer is wholly responsible to the Board for the day to day running of the Group. The collective responsibility of the Group's management is vested in the Chief Executive Officer and bears ultimate responsibility for all management functions.

The Chief Executive Officer undertakes the following key responsibilities:

a) Ensures that the policies spelt out by the Board in the Group's overall corporate strategy of the institution are implemented;
b) Identifies and recommends to the Board competent officers to manage the operations of the Group;
c) Establishes and maintains efficient and adequate internal control systems; and
d) Ensures that the Board is frequently and adequately appraised about the operations of the Group.

In addition to the Managing Director, Executive Directors and members of senior management of the Company attend Board Meetings by invitation to ensure informed and efficient decision-making by the Board of Directors. Further, the Board invites third party professionals to attend Meetings and provide opinions and advice when necessary to enable the Board discharge its fiduciary mandate.

The Board is assisted by a qualified and competent company secretary of good standing with the Institute of Certified Public Secretaries of Kenya (ICPSK);

The Group's strategies are sustainable; and it has clearly identified the Directors' fiduciary duties.

CORPORATE GOVERNANCE STATEMENT (Continued)

5. BOARD LEADERSHIP AND RESPONSIBILITY OF THE BOARD

The Board recognises its responsibility to provide effective leadership based on an ethical foundation. This involves responsible leadership characterized by the ethical values of responsibility, accountability, fairness and transparency all of which are enshrined in our core values. The Board Charter sets out the responsibilities of the Board which include:

- The provision of strategic guidance and effective oversight of management and maximization of the Group's financial performance and shareholder value within the framework of appropriate risk assessment.
- The provision of the overall direction, governance and promoting proper standards of conduct and sound banking practices which enhance internal controls and shareholder value.
- Cognisant of its responsibility for defining appropriate governance practices and to ensure that such practices are followed and periodically reviewed for improvement, the Board has met at regular intervals to, amongst others things:
- Agree on the Bank's strategic objectives, and its roadmap to achieving the agreed objectives,
- Review and approve the Bank's annual budget,
- Review the Bank's performance against approved budget,
- Review the Bank's policies and procedures,
- Consider and approve the annual and interim financial statements,
- Recommend dividends to the shareholders,
- Evaluate the performance of the Managing Director, and
- Approve other matters of fundamental significance.

5.1. Principle on Appointment, Composition, Size and Qualifications of Board Members

The Board has appointed a Nominations Committee, which proposes new members for Board appointment, as well as spearheading Board evaluation. In proposing appointments to the Board, the Committee ensures the achievement of diversity in its composition, as well as ensuring that at least three-fifths of the Directors are Non-executive and at least one third of the total number of Directors are Independent. The Board's composition is not biased towards representation of a substantial shareholder of the Group, but instead, it reflects the Group's broad shareholding structure.

The Board's composition provides a mechanism for representation of any minority shareholders without undermining the collective responsibility of the Directors.

5.2. Principle on the Functions of the Board

To enhance accountability to its Shareholders, the Group has ensured that:

i) It has distinguished the roles reserved for the Board and those delegated to Management;
ii) The functions of the Chairperson and the Chief Executive Officer are not exercised by the same individual;

5.3. Principle on Age Limit for Board Members

The Code Of Corporate Governance Practices for Issuers of Securities to the Public 2015 has prescribed 70 years as the age limit for its Directors. Any Director who has reached the age of 70 years resigns from the office of Director at the following Annual General Meeting and Shareholders are informed of such resignation at each Annual General Meeting. If any Director wishes to continue serving in the office of Director, he/she must seek the approval of the Shareholders at an Annual General Meeting.

5.4. Principle on Board Tools

The Group has developed a Code of Ethics and Conduct, which will be cascaded down to all employees. It already has an established a Board Charter to guide in the activities of the Board. Further, the Board develops a work plan and an evaluation toolkit annually, to ensure effectiveness.

CORPORATE GOVERNANCE STATEMENT (Continued)

5.5. Principle on Governance and Legal Audit

The Board has mandated the Group to conduct an annual governance audit, in order to assess the level of compliance with sound governance practices. Additionally, a compliance and legal audit is conducted to identify the level of compliance with applicable laws, regulations and standards. The 2018 Legal self- audit was successfully completed during the year. Procurement of a service provider to conduct Governance Audit is underway.

5.6. Compliance with Laws and Regulations

Family Bank has a listed Medium Term Note in the Fixed Securities Segment of the Nairobi Securities Exchange (the Exchange) and as such, is bound by and complies with:

a) The Capital Markets Act Cap. 485 and all subsidiary legislation made thereunder;
b) The NSE rules and guidelines issued by the Capital Markets Authority (the Authority), the Exchange and any requirements, decisions or directions given by the Authority and the Exchange;
c) The Banking Act and all prudential guidelines and directions given by the Central Bank of Kenya and other regional regulators;
d) The Kenya Companies Act, No. 17 of 2015 and its amendments thereto; and
e) All other applicable laws and regulations governing the various lines of businesses it is engaged in.

5.7. Risk Management

Why it matters

As a large financial services organization operating in a complex industry, effective risk management is critical to the overall profitability, competitive market positioning and long-term financial viability of the Company.

Our Risk Management Framework sets out lines of responsibility and authority for risk-taking, governance and control. The Board of Directors is ultimately responsible for ensuring the oversight of all risks across the enterprise and has primary responsibility for taking action to ensure risk management policies, programs and practices are in place.

The Board delegates certain responsibilities to standing Board Committees, which oversee and monitor these risks:

- Risk Management and Compliance Committee
- Audit Committee

Our approach

We have a Risk Management Framework, approved by the Board of Directors that prescribes a comprehensive set of protocols and programs for conducting our business activities. This framework seeks to ensure that risks to a business undertaking are appropriately managed to achieve the Company's business objectives over time. The Risk Management Framework, corporate strategy and business objectives are all aligned and risk management protocols and programs are embedded in every business segment.

Our Risk Appetite Policy, also approved by the Board of Directors, sets out specific constraints that define the aggregate level of risk that the Company is willing to accept. The Company's risk appetite seeks to balance the various needs, expectations, risk and reward perspectives and investment horizons of key stakeholders. In particular, our risk appetite supports the pursuit of shareholder value while ensuring that the Company's ability to pay claims and fulfil policyholder commitments is not compromised.

Our risk management program is embedded in the Company's culture, which encourages ownership and responsibility for risk management at all levels. A key premise is that all employees have an important role to play in managing the Company's risks.

Assurance is guaranteed via risk department, internal audit, compliance and enforcement teams, external audits by PwC, Central Bank Audit, Capital Markets Authority and Nairobi Securities Exchange reviews.

CORPORATE GOVERNANCE STATEMENT (Continued)

6. BOARD ACTIVITIES 2018

6.1. Board attendance

The Board convened 8 board meetings during the year. All the meetings convened had sufficient quorum. The attendance of the individual directors was as follows:

Directors	Total Attendance
Wilfred D. Kiboro (Chairman)	100%
T.K. Muya	100%
Lazarus Muema	100%
Ruth Waweru	100%
Francis Mungai	71%
Lerionka Tiampati	100%
David Thuku	100%

6.2. Board Training and Continuous Professional Development 2018

During the year, the Board members attended training on Corporate Governance as part of Continuous Professional Development and in line with CBK Prudential Guideline on Corporate Governance. There was also training on Board Risk committee members undertook training in cybersecurity while Board Audit Committee members took training on Integrated reporting.

6.3. Board Evaluation

The annual Board evaluation was conducted in March 2019 in a process led by the Chairman to the Board and supported by the Company Secretary. The Board conducted the process internally and engaged an analyst to compile the results of the evaluation.

The evaluation entailed an evaluation of the Board, peer evaluation for each director, evaluation of the Chair to the Board and the Board Committees It covered overall Board interactions, conduct of board meetings and scope of control exercised by the directors. Following the exercise, the directors identified areas that required further consideration by the Board and these issues have been captured in the rolling agenda.

7. COMMITTEES OF THE BOARD

The Board has six Committees with specific delegated authorities. These are the Board Audit Committee, the Board Risk Management Committee, the Board Credit Committee, the Board Nomination Committee, Board Strategy Committee and the Human Resources Committee. Three of the five committees are mandatory from a regulatory perspective while three have been established to provide dedicated oversight on specific key functions of the bank. Board Committee members are appointed by the Board which also reviews the composition of each Committee regularly.

7.1. Board Audit Committee

The Committee reviews the integrity of the financial statements of the Company and its subsidiaries and recommends the statements for approval to the Board, the effectiveness of the Company's system of internal control and receives reports on the findings of the internal and external audits and tracks the actions on audit findings. The Committee also reviews the proposed work plans for the Internal Audit and Compliance functions at the beginning of each year.

CORPORATE GOVERNANCE STATEMENT (Continued)

COMMITTEES OF THE BOARD (CONTINUED)

7.1. Board Audit Committee (Continued)

The Committee held six meetings during the year under review. The members of this committee during the year under review were Mr. Lazarus Muema (Chairman), Dr. Ruth Waweru and Mr Lerionka Tiampati. The Head of Internal Audit attended all Committee meetings.

7.2. Board Credit Committee

The Credit Committee plays a critical role in the formulation and review of lending policies and ensures that such policies are in compliance with regulatory requirements. It assesses the credit quality and risk profile of the Bank's lending book by sector and by product and makes recommendations to the Board on remedial actions or on matters that may enhance the quality of the lending book.

The Committee met two times during the year under review. The members of the Committee in the year under review were: Mr. Francis Mungai (Chairman), Dr. W. D. Kiboro, Mr. T.K. Muya, Dr. David Thuku. The Head of Credit attended all Committee meetings.

7.3. Board Risk Management Committee

The Committee oversees the group's preparedness and mitigation for the major risks faced by the Group across the business including operational risk, country risk, credit risk, liquidity risk, market risk, regulatory risk, legal risk, reputational risk and compliance risk. The Committee is responsible for ensuring that there are written policies, procedures and processes for identifying and managing the risks.

The Committee met four times during the year and recorded a quorum during all its meetings. The members of the Committee in the year under review were Mr. Lazarus Muema (Chairman) and Dr. Ruth Waweru, Mr. L. Tiampati. The Head of Risk and Compliance attended all Committee meetings.

7.4. Board Human Resource Committee

The Committee acts as the link between the Board and management and is responsible for the review of the human resources policies and practices, particularly in relation to the operations of the various business units. The Committee also assists the Managing Director in Human Resources Management and act as a medium of key management staff and new Board members' recruitment and ensures that the organisational structure supports the business strategy and growth.

The Committee met twice times during the year under review. The members of the Committee are which is Chaired by Dr. R.Waweru are Mr. T. K Muya, Mr. Francis Mungai, Dr. W.D. Kiboro, and Dr. David Thuku. The Director Human Resources attended all the Committee meetings.

7.5. Board Strategy Committee

The Committee analyses the strategy of the Group and provides oversight over the implementation of the strategy approved by the Board by reviewing progress on a regular basis. They review the budget and strategic plan of the Group prior to submission to the Board.

The Committee met three times during the year and achieved sufficient quorum in all its meetings. The members of the Committee are; Dr. Ruth Waweru (Chairman), Dr. W.D. Kiboro, Mr. T. K. Muya, Mr. Lerionka Tiampati, and Dr. David Thuku. The Head of Strategy and other members of management attend the meetings of the Committee.

CORPORATE GOVERNANCE STATEMENT (Continued)

7. COMMITTEES OF THE BOARD (CONTINUED)

7.6. Board Nomination Committee

The Committees regularly reviews the structure, size and composition of the board and make recommendations on any adjustments deemed necessary. It identifies, nominates and recommends for the approval of the board, candidates to fill board vacancies as and when they arise. The Committee members are; Dr Ruth Waweru (Chairman), Dr. W. D. Kiboro and Mr. T.K. Muya. This committee held one meeting in 2018.

8. BOARD PERFORMANCE

The Board had full access to corporate information and sufficient detail to enable a productive and open discussion. There is diversity in the Board which ensures that the level of debate is both detailed and of a high technical standard. Overall, the Board's performance was efficient and effective, leading to the remarkable performance of the Group in all parameters during the year.

9. CAPITAL STRUCTURE

a) Share Capital

The authorised and issued share capital of Family Bank Limited consists of only ordinary shares as disclosed on note 30 to the financial statements.

b) Top Ten Shareholders as at 31 December 2018

No	Shareholder	No. of Shares
1	Kenya Tea Development Agency Holding Ltd	212,184,905
2	Rachael Muya	167,143,948
3	Daykio Plantations Limited	158,460,364
4	Titus Kiondo Muya	70,025,530
5	Standard Chartered Kenya Nominees Ltd a/c 9660b	46,417,000
6	PA Securities	44,444,445
7	Julius Muya Kiondo	33,448,788
8	Ann Muya	33,428,788
9	Mark Keriri	33,428,788
10	Sheila Muindi	33,428,788
	Top 10 Shareholders	832,411,344
	Others	454,696,198
	Total Issued Shares	1,287,107,542

CORPORATE GOVERNANCE STATEMENT (Continued)

9. CAPITAL STRUCTURE (Continued)

c) Distribution of Shareholders as at 31st December 2018

	No of Shareholders	No of Shares	%
10,000,000 - Above	17	992,007,502	77.07%
50,000 - 9,999,999	623	239,678,704	18.62%
10,000 - 49,999	2,079	38,070,828	2.96%
1 - 9,999	3,221	17,350,506	1.35%
Total	5,940	1,287,107,542	100.00%

d) Directors Holding Shares as at 31st December 2018

Name	No. of shares	%
Wilfred Kiboro	11,893,168	0.924%
Titus Muya	70,025,530	5.441%
Dr. Ruth Waweru	190,000	0.015%
Francis Mungai	1,620,404	0.126%
Lazarus Muema	49,000	0.004%
Total	83,778,102	6.509%

REPORT OF THE DIRECTORS

The directors submit their report together with the audited financial statements for the year ended 31 December 2018, which disclose the state of affairs of Family Bank Limited (the "Bank" or the "Company") and its subsidiary, Family Bank Insurance Agency Limited (together "the Group").

PRINCIPAL ACTIVITIES

The Group provides an extensive range of banking, financial and related services and is licensed under the Banking Act. The principal activity of the subsidiary is to provide bancassurance services through insurance agency services.

BUSINESS REVIEW

The Group recorded a significantly improved performance from a loss after tax of Ksh 1b in 2017 to a profit after tax of Ksh 244m in 2018. The Business model review and process refinement undertaken in the last two years is now generating the envisaged efficiencies and business growth. This is evidenced by the 19% or Ksh 1.3b reduction in expenses and a 3% revenue growth while our deposits and loans and advances to customers registered a 2% growth. The Board is confident that the Group is now firmly back on a growth trajectory and the positive results will be sustained into the future.

The following is the summary of the results for the year ended 31 December 2018:

	Group		Bank	
	2018	2017	2018	2017
	Sh'000	Sh'000	Sh'000	Sh'000
Profit/ (Loss) before taxation	434,932	(1,357,638)	419,880	(1,370,841)
Taxation	(190,716)	356,850	(185,034)	361,264
Profit/ (Loss) for the year	244,216	(1,000,788)	234,846	(1,009,577)

DIVIDEND

The directors do not recommend payment of a dividend in respect of the year ended 31 December 2018 (2017: Nil).

DIRECTORS

The Directors who held office at the date of this report are set out on pages 9 to 12.

Dr. David Thuku served as the Managing Director and CEO during part of the year until 15 November 2018.

EVENTS SUBSEQUENT TO THE END OF THE REPORTING PERIOD

There were no material subsequent events after the reporting date requiring disclosure in these financial statements as at the date of the financial statement approval.

REPORT OF THE DIRECTORS

STATEMENT AS TO DISCLOSURE TO THE COMPANY'S AUDITOR

With respect to each director at the time this report was approved:

(i) there is, so far as the director is aware, no relevant audit information of which the Company's auditor is un aware; and

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

TERMS OF APPOINTMENT OF AUDITOR

PricewaterhouseCoopers continue in office in accordance with the Company's Articles of Association and Section 719 of the Kenyan Companies Act, 2015.

The directors monitor the effectiveness, objectivity and independence of the auditor. This responsibility includes the approval of the audit engagement contract and the associated fees on behalf of the shareholders.
By order of the Board

COMPANY SECRETARY
25th March 2019

STATEMENT OF DIRECTORS RESPONSIBILITIES

The Kenyan Companies Act 2015 requires the directors to prepare financial statements for each financial year which give a true and fair view of the financial position of the Group and Company at the end of the financial year and its financial performance for the year then ended. The directors are responsible for ensuring that the Group and Company keeps proper accounting records that are sufficient to show and explain the transactions of the Group and Company; disclose with reasonable accuracy at any time the financial position of the Group and Company; and that enables them to prepare financial statements of the Group and Company that comply with prescribed financial reporting standards and the requirements of the Kenyan Companies Act 2015. They are also responsible for safeguarding the assets of the Group and Company and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

i. Designing, implementing and maintaining internal control as they determine necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error;

ii. Selecting suitable accounting policies and then apply them consistently; and

iii. Making judgements and accounting estimates that are reasonable in the circumstances

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

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

Approved by the board of directors on 25th March 2019 and signed on its behalf by:

Dr. Wilfred D. Kiboro
Chairman

Lazarus Muema
Director

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF FAMILY BANK LIMITED

Report on the audit of the financial statements

Our opinion

We have audited the accompanying financial statements of Family Bank Limited (the Bank or Company) and its subsidiary (together, the Group) set out on pages 51 to 127, which comprise the consolidated statement of financial position at 31 December 2018 and the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, together with the Bank statement of financial position at 31 December 2018 and the Bank statements of comprehensive income, changes in equity and cash flows for the year then ended, and the notes to the financial statements, including a summary of significant accounting policies.
In our opinion the accompanying financial statements of Family Bank Limited give a true and fair view of the financial position of the Group and the Bank at 31 December 2018 and of their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act, 2015.

Basis for opinion

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

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters

PricewaterhouseCoopers CPA. PwC Tower, Waiyaki Way/Chiromo Road, Westlands
P O Box 43963 – 00100 Nairobi, Kenya
T: +254 (20)285 5000 F: +254 (20)285 5001 www.pwc.com/ke

Partners: E Kerich B Kimacia M Mugasa A Murage F Muriu P Ngahu R Njoroge S O Norbert's B Okundi K Saiti
Key audit matters

Key audit matter	*How our audit addressed the matter*
Credit risk and provision for expected credit losses on financial assets (continued) The Group implemented IFRS 9: Financial instruments on 1 January 2018. The standard requires the Group to recognise expected credit losses (ECLs) on financial assets, both on-balance sheet and off-balance sheet. As explained in note 3 (a) of the financial statements, the estimation of expected credit losses on financial instruments is complex and judgmental, and involves a high degree of estimation uncertainty. The following inputs in the estimation of the expected credit losses on financial instruments require significant judgment and assumptions by management: • estimation of default events that may happen during the lifetime of the instruments, and the probability weighting thereof; • identifying exposures that have experienced significant increase in credit risk (SICR) or met the Group's default criteria; In addition, the calculation of the expected credit losses on financial instruments requires complex mathematical models and modelling assumptions.	We obtained an understanding of the Bank's IFRS 9 implementation process including the governance processes thereof through discussions with management and review of related documentation. We reviewed and assessed management's accounting policies over key IFRS 9 concepts especially SICR, default definition, forecasting of forward looking macro-economic factors, and weighting of expected loss scenarios. For a sample of financial instruments' contracts, we tested the identification of financial assets that have experienced SICR or met the Group's default definition criteria for purposes of staging, by examining documentation and credit performance to form an independent judgment as to whether the staging of such facilities was in line with the Group's policy. For stage 3 facilities, we selected a sample of financial assets and examined the reasonableness of the expected future recoverable amounts as assessed by management to support the calculation of the ECL thereon. We assessed the assumptions and compared estimates to both internal and external evidence, where available. Where impairment was calculated using a model (stages 1 & 2), we tested the basis and operation of those models and the data and assumptions used. Our audit procedures included: • Comparison of the principal assumptions made with our own knowledge of other practices and actual experience. • Testing the operation of the models used to calculate the impairment including, in some cases, developing independent expectations and comparing results. • Assessed overlays made by management over and above the formulaic computed ECLs We also reviewed management's ECL related disclosures in the financial statements especially on transition impact, as well as the areas with the highest estimation levels.

Other information

The other information comprises Corporate information, Directors' report and the Statement of Directors' responsibilities which we obtained prior to the date of this auditor's report, and the rest of the other information in the Annual Report which are expected to be made available to us after that date, but does not include the financial statements and our auditor's report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information we have received prior to the date of this auditor's report we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the rest of the other information in the Annual Report and we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

Responsibilities of the directors for the financial statements

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

In preparing the financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

Auditor's responsibilities for the audit of the financial statements (continued)

- Conclude on the appropriateness of the directors' 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 Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group 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 of the entities or business activities within the Group to express an opinion on the Group's financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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

Report on other matters prescribed by the Kenyan Companies Act, 2015

Directors' Report

In our opinion the information given in the Directors' Report on pages 44 and 45 is consistent with the financial statements.

Certified Public Accountants
Nairobi
28th March 2019

CPA Kang'e Saiti, Practising certificate No. 1652
Signing partner responsible for the independent audit

STATEMENT OF COMPREHENSIVE INCOME

	Notes	Group 2018 Sh'000	Group 2017 (Restated)* Sh'000	Bank 2018 Sh'000	Bank 2017 (Restated)* Sh'000
Interest income	6	7,056,590	7,560,922	7,056,590	7,560,922
Interest expense	7	(2,283,914)	(2,667,882)	(2,289,719)	(2,674,118)
Net interest income		4,772,676	4,893,040	4,766,871	4,886,804
Foreign exchange gains		337,455	288,761	337,456	288,761
Fee and commission income	8(a)	2,038,214	1,779,944	2,038,214	1,779,944
Other income	8(b)	123,303	104,497	59,021	33,134
Operating income		7,271,648	7,066,242	7,201,562	6,988,643
Operating expenses	9	(5,632,443)	(6,979,418)	(5,577,409)	(6,915,022)
Credit impairment losses	16 (c)	(1,204,273)	(1,444,462)	(1,204,273)	(1,444,462)
Profit/ (loss) before taxation		434,932	(1,357,638)	419,880	(1,370,841)
Income tax credit / (expense)	11	(190,716)	356,850	(185,034)	361,264
Profit/ (loss) for the year		244,216	(1,000,788)	234,846	(1,009,577)
Realised fair value adjustments on available for sale investments transferred to profit or loss		-	1,007	-	1,007
		-	1,007	-	1,007
Total other comprehensive income		-	1,007	-	1,007
Total comprehensive income for the year		244,216	(999,781)	234,846	(1,008,570)
Earnings per share (basic and diluted) (Shs)	12	0.20	(0.80)	0.19	(0.81)

STATEMENT OF FINANCIAL POSITION

	Notes	Group 2018 Sh'000	Group 2017 Sh'000	Bank 2018 Sh'000	Bank 2017 Sh'000
ASSETS					
Cash and balances with Central Bank of Kenya	13	6,281,701	5,641,710	6,281,701	5,641,710
Balances due from banking institutions	14(a)	1,222,738	2,495,298	1,222,738	2,495,298
Government securities amortised cost	15	6,946,277	7,692,403	6,946,277	7,692,403
Corporate bonds at amortised cost	17	392,772	842,679	392,772	842,679
Other investments	19	1,730,698	1,830,097	1,730,698	1,830,097
Loans and advances to customers	16	44,113,093	43,471,853	44,113,093	43,471,853
Other assets	18	1,607,838	1,786,662	1,567,670	1,748,148
Investment in subsidiary	20	-	-	1,000	1,000
Investment properties	21	18,200	18,200	18,200	18,200
Property and equipment	22	2,841,773	3,622,587	2,837,332	3,615,785
Intangible assets	23	597,692	470,887	575,323	465,526
Prepaid operating leases	24	143,885	148,736	143,885	148,736
Current income tax	11	587,095	788,944	551,846	755,013
Deferred tax asset	29	527,303	324,879	527,303	324,495
TOTAL ASSETS		67,011,065	69,134,935	66,909,838	69,050,943
LIABILITIES AND SHAREHOLDERS' FUNDS					
LIABILITIES					
Customer deposits	25	48,483,189	47,362,130	48,558,691	47,425,108
Balances due to banking institutions	14(b)	247,051	201,708	247,051	201,708
Borrowings	26	4,903,207	8,362,529	4,903,207	8,362,529
Provisions	27(a)	349,615	313,340	349,615	312,655
Other liabilities	27(b)	1,446,678	1,141,964	1,424,826	1,140,650
Deferred tax liability	29	535	-		-
TOTAL LIABILITIES		55,430,275	57,381,671	55,483,390	57,442,650
SHAREHOLDERS' FUNDS					
Share capital	30	1,287,108	1,287,108	1,287,108	1,287,108
Share premium	30	5,874,662	5,874,662	5,874,662	5,874,662
Revaluation surplus		192,624	192,624	192,624	192,624
Retained earnings		4,226,396	4,102,941	4,072,054	3,957,970
Statutory reserve		-	295,929	-	295,929
TOTAL SHAREHOLDERS' FUNDS		11,580,790	11,753,264	11,426,448	11,608,293
TOTAL LIABILITIES AND SHAREHOLDERS' FUNDS		67,011,065	69,134,935	66,909,838	69,050,943

The financial statements on pages 51 to 127 were approved for issue by the board of directors on 25th March 2019 and were signed on its behalf by:

Dr. Wilfred D. Kiboro
Director

Lazarus Muema
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Note	Share capital Sh'000	Share premium Sh'000	Revaluation surplus Sh'000	Fair value reserves Sh'000	Retained earnings Sh'000	Statutory reserve Sh'000	Total Sh'000
At 1 January 2017		1,287,108	5,874,662	195,888	1,007	4,954,665	441,729	12,755,059
Comprehensive income for the year								
Loss for the year		-	-	-	-	(1,000,788)	-	(1,000,788)
Other comprehensive income, net of tax		-	-	-	(1,007)	-	-	(1,007)
Other movements								
Transfer from statutory reserve		-	-	-	-	145,800	(145,800)	-
Transfer of excess depreciation		-	-	(4,663)	-	4,663	-	-
Deferred tax on excess depreciation		-	-	1,399	-	(1,399)	-	-
At 31 December 2017		1,287,108	5,874,662	192,624	-	4,102,941	295,929	11,753,264
		======	======	======	======	======	======	======
At 1 January 2018		1,287,108	5,874,662	192,624	-	4,102,941	295,929	11,753,264
Impact of initial application of IFRS 9	2B	-	-	-	-	(120,761)	(295,929)	(416,690)
		1,287,108	5,874,662	192,624	-	3,982,180	-	11,336,574
Comprehensive income for the year								
Profit for the year		-	-	-	-	244,216	-	244,216
At 31 December 2018		1,287,108	5,874,662	192,624	-	4,226,396	-	11,580,790
		=======	=======	=======	=======	=======	=======	=======

BANK STATEMENT OF CHANGES IN EQUITY

		Share capital Sh'000	Share premium Sh'000	Revaluation surplus Sh'000	Fair value reserves Sh'000	Retained earnings Sh'000	Statutory reserve Sh'000	Total Sh'000
At 1 January 2017		1,287,108	5,874,662	195,888	1,007	4,818,483	441,729	12,618,877
Comprehensive income for the year								
Loss for the year		-	-	-	-	(1,009,577)	-	(1,009,577)
Other comprehensive income, net of tax		-	-	-	(1,007)	-	-	(1,007)
Other movements								
Transfer from statutory reserve		-	-	-	-	145,800	(145,800)	-
Transfer of excess depreciation		-	-	(4,663)	-	4,663	-	-
Deferred tax on excess depreciation				1,399		(1,399)		
At 31 December 2017		1,287,108	5,874,662	192,624	-	3,957,970	295,929	11,608,293
At 1 January 2018		1,287,108	5,874,662	192,624	-	3,957,970	295,929	11,608,293
Impact of initial application of IFRS 9	2B	-	-	-	-	(120,762)	(295,929)	(416,691)
		1,287,108	5,874,662	192,624	-	3,837,208	-	11,191,602
Comprehensive income for the year								
Profit for the year		-	-	-	-	234,846	-	234,846
At 31 December 2018		1,287,108	5,874,662	192,624	-	4,072,054	-	11,426,448

STATEMENT OF CASH FLOWS

	Note	Group 2018 Sh'000	Group 2017 Sh'000	Bank 2018 Sh'000	Bank 2017 Sh'000
Cash flows from operating activities					
Net cash generated from operations	31(a)	2,376,371	8,777,284	2,372,973	8,777,903
Taxation paid	11(c)	(12,707)	(4,990)	(6,093)	(4,990)
Cash generated from operating activities		2,363,664	8,772,295	2,366,880	8,769,913
Cash flows from investing activities					
Purchase of property and equipment	22	(28,412)	(220,200)	(28,412)	(218,706)
Purchase of intangible assets	23	(19,679)	(162,942)	(19,679)	(161,504)
Proceeds on sale of motor vehicles		-	16,480	-	15,930
Net cash used in investing activities		(48,091)	(366,662)	(48,091)	(364,280)
Cash flows from financing activities					
Borrowings received	26	2,211	7,931	2,211	7,931
Short term borrowings from Central Bank		-	(4,393,608)	-	(4,393,608)
Repayment of borrowings	26	(3,623,759)	(898,045)	(3,623,759)	(898,045)
Dividends paid	28	-	(1,912)	-	(1,912)
Net cash generated from financing activities		(3,621,548)	(5,285,634)	(3,621,548)	(5,285,634)
Net increase in cash and cash equivalents during the period		(1,305,975)	3,119,999	(1,302,759)	3,119,999
Cash and cash equivalents at year start		5,776,023	2,656,024	5,776,023	2,656,024
Cash and cash equivalents at end year	31(b)	4,470,048	5,776,023	4,470,048	5,776,023

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2018

1. General information

Family Bank Limited and its subsidiary Family Insurance Agency Limited are both incorporated in Kenya under the Companies Act and is domiciled in Kenya.

For Kenyan Companies Act reporting purposes, the balance sheet is represented by the statement of financial position and the profit and loss account by the statement of comprehensive income, in these financial statements.

2. Significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

a) Basis of preparation

(i) Basis of measurement

The financial statements are prepared in compliance with International Financial Reporting Standards (IFRS) applicable to companies reporting under IFRS and in accordance with the Kenyan Companies Act, 2015. The financial statements are presented in thousands of Kenya shillings rounded to the nearest thousand (Shs '000) and are prepared under the historical cost convention as modified by the revaluation of financial assets at fair value through other comprehensive income and financial assets and liabilities (including derivative instruments) at fair value through profit or loss.

(ii) Use of estimates

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates and assumptions. It also requires the directors to exercise judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or where assumptions and estimates are significant to the financial statements, are disclosed in note 4.

(iii) Changes in accounting policies and disclosures

(a) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

A number of new standards and interpretations have been published that are not mandatory for annual periods commencing 1 January 2018 and have not been early adopted by the Group. The Group's assessment of the impact of these new standards and interpretations is as follows:

IFRS 16: Leases

The standard was issued in January 2016 and replaces the existing standard on leases i.e. IAS 17. It will result in almost all leases being recognised on the statement of financial position, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short-term and low-value leases. The accounting for lessors will not significantly change.

The standard will affect primarily the accounting for Group's operating leases. As at the reporting date, the Group has non-cancellable operating lease commitments of Shs 5,012 million (2017: Shs 4,937 million) (see Note 33). However, the Group is still in the process of performing a comprehensive review of its leases, from which exercise, it will determine right of use asset and related liability for future payments, to be recognised.

Some of the commitments may be covered by the exception for short-term and low-value leases and some commitments may relate to arrangements that will not qualify as leases under IFRS 16. The standard is effective for annual periods beginning on or after 1 January 2019. The Group is currently assessing the impact of the standard on its financial statements. The actual impact of applying IFRS 16 on the financial statements for the financial year ending 31 December 2019 will depend on: (a) the final reconciliation of the of the Group's leases' portfolio; (b) the Group's assessment of whether it will exercise any lease renewal options; and (c) the extent to which the Group chooses to utilise practical expedients and recognition exemptions available under the standard especially on the low value and short term leased assets.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2018

2. Significant accounting policies (continued

(iii) Changes in accounting policies and disclosures

(a) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group (continued)

IFRS 16: Leases (continued)

On transition, IFRS 16 allows entities not to restate its comparatives. The Group will therefore adopt IFRS 16 on 1 January 2019 using a modified retrospective approach. As such, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

(b) New and amended standards effective and adopted by the Group

The following standards have been applied by the Group for the first time for the financial year beginning 1 January 2018:

- Various amendments with no or immaterial impact
- Classification and measurement of share-based payment transactions – amendments to IFRS 2
- Annual improvements 2015 - 2017 cycle
- Transfers of investment property – amendments to IAS 40
- Interpretation 22 foreign currency transactions and advance consideration

IFRS 15: Revenue from contracts with customers

This standard became effective on 1 January 2018 and replaced the existing revenue standards and their related interpretations. The standard sets out the requirements for recognising revenue that applies to all contracts with customers, except for contracts that are within the scope of the standards on financial instruments, leases and insurance contracts.

The core principle of the standard is that revenue recognised reflects the consideration to which the company expects to be entitled in exchange for the transfer of promised goods or services to the customer. The standard incorporates a five step analysis to determine the amount and timing of revenue recognition.

Because the standard does not apply to revenue associated with financial instruments, it does not impact the majority of the Group's revenue streams. The Group identified and reviewed the contracts with customers that are within the scope of this standard and concluded that the adoption of IFRS 15 did not materially impact the Group's revenue recognition criteria and there were therefore no transition adjustments required.

IFRS 9: Financial Instruments

The Group adopted IFRS 9 as issued by the IASB in July 2014 effective 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements. The Group did not early adopt any of IFRS 9 in previous periods.

As permitted by the transitional provisions of IFRS 9, the Group elected not to restate comparative figures. Any adjustments to the carrying amounts of financial assets and financial liabilities at the date of transition were recognised in the opening retained earnings and other reserves of the current period.

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

The adoption of IFRS 9 has resulted in changes in our accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7 'Financial Instruments: Disclosures'.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

a) Basis of preparation (continued)

(iii) Changes in accounting policies and disclosures (continued)

IFRS 9: Financial instruments (continued)

Set out below are disclosures relating to the impact of the adoption of IFRS 9 on the Group.

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Group's and Company's financial assets and financial liabilities as at 1 January 2018.

Group

A. Classification and measurement of financial instruments

	Original classification under IAS 39	New classification under IFRS 9	Carrying amount under IAS 39	New carrying amount under IFRS 9
Financial assets			Shs ' 000	Shs ' 000
Balances with Central Bank of Kenya	Loans and receivables	Amortised cost	2,159,276	2,159,276
Balances due from financial institutions	Loans and receivables	Amortised cost	2,495,298	2,495,089
Government securities	Held to maturity (HTM)	Amortised cost	7,692,403	7,692,403
Corporate bonds	HTM	Amortised cost	842,679	828,086
Loans and advances from customers	Loans and receivables	Amortised cost	43,471,853	42,894,291
Other investments	Loans and receivables	Amortised cost	1,830,097	1,827,231
Other assets (financial)	Loans and receivables	Amortised cost	1,258,692	1,258,692
Total financial assets			**59,750,298**	**59,155,068**
			========	========
Financial liabilities				
Customers deposits	Amortised cost	Amortised cost	47,362,130	47,362,130
Borrowed funds and due to banking institutions	Amortised cost	Amortised cost	8,564,237	8,564,237
Other liabilities (financial)	Amortised cost	Amortised cost	1,076,637	1,076,637
Total financial liabilities			**57,003,004**	**57,003,004**
			========	========

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

a) Basis of preparation (continued)

(iii) Changes in accounting policies and disclosures (continued)

IFRS 9 Financial instruments (continued)

A. Classification of financial instruments (continued)

Bank

	Original classification under IAS 39	New classification under IFRS 9	Carrying amount under IAS 39	New carrying amount under IFRS 9
Financial assets			Shs ' 000	Shs ' 000
Balances with Central Bank of Kenya	Loans and receivables	Amortised cost	2,159,276	2,159,276
Balances due from financial institutions	Loans and receivables	Amortised cost	2,495,298	2,495,089
Government securities	Held to maturity (HTM)	Amortised cost	7,692,403	7,692,403
Corporate bonds	HTM	Amortised cost	842,679	828,086
Loans and advances from customers	Loans and receivables	Amortised cost	43,471,853	42,894,291
Other investments	Loans and receivables	Amortised cost	1,830,097	1,827,231
Other assets (financial)	Loans and receivables	Amortised cost	1,220,179	1,220,179
Total financial assets			**59,711,785**	**59,116,555**
			========	========
Financial liabilities				
Customers deposits	Amortised cost	Amortised cost	47,425,108	47,425,108
Borrowed funds and due to banking institutions	Amortised cost	Amortised cost	8,564,237	8,564,237
Other liabilities (financial)	Amortised cost	Amortised cost	1,075,323	1,075,323
Total financial liabilities			**57,064,668**	**57,064,668**
			========	========

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

a) Basis of preparation (continued)

(iv) Changes in accounting policies and disclosures (continued)

IFRS 9 Financial instruments (continued)

B. Reconciliation of statement of financial position balances from IAS 39 to IFRS 9

The Group performed an analysis of its business models for managing financial assets as well as the assets' cash flow characteristics. Further detailed information regarding the new classification of financials assets under IFRS 9 is provided in Note 2(b). Overall, loans and receivables and held to maturity financial investments (measured at amortised cost under IAS 39) were classified as financial assets at amortised cost (under IFRS 9). The Group did not hold financial assets at fair value through profit or loss and other comprehensive income at transition date

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Group's financial assets and financial liabilities on 1 January 2018. Remeasurement adjustments arising upon the application of IFRS 9 principles are also presented in the reconciliation.

Group

Financial assets	IAS 39 carrying amount 31 December 2017 Shs ' 000	Reclassification Shs ' 000	Remeasurement Shs ' 000	IFRS 9 carrying amount 1 January 2018 Shs ' 000
Amortised cost:				
Balances with Central Bank of Kenya: Opening balance as per IAS 39 and closing balance as per IFRS 9	2,159,276	-	-	2,159,276
Balances with other financial institutions				
Opening balance as per IAS 39	2,495,298	-	-	-
Remeasurement: ECL allowance	-	-	(209)	-
Closing balance as per IFRS 9	-	-	-	2,495,089
Government securities: Opening balance as per IAS 39 and closing balance as per IFRS 9	7,692,403	-	-	7,692,403
Corporate bond investments				
Opening balance as per IAS 39	842,679	-	-	-
Remeasurement: ECL allowance	-	-	(14,593)	-
Closing balance as per IFRS 9	-	-	-	828,086
Customer loans and advances				
Opening balance as per IAS 39	43,471,853	-	-	-
Remeasurement: ECL allowance		-	(577,562)	-
Closing balance as per IFRS 9		-	-	42,894,291
Other investments				
Opening balance as per IAS 39	1,830,097	-	-	-
Remeasurement: ECL allowance	-	-	(2,866)	-
Closing balance as per IFRS 9	-	-	-	1,827,231
Other assets: Opening balance as per IAS 39 and closing balance as per IFRS 9	1,258,692	-	-	1,258,692
Total financial assets measured at amortised cost	**59,750,298**	**-**	**(595,230)**	**59,155,068**
	========	========	========	========

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

b) Basis of preparation (continued)

(v) Changes in accounting policies and disclosures (continued)

IFRS 9 Financial instruments (continued)

B. Reconciliation of statement of financial position balances from IAS 39 to IFRS 9 (continued)

Bank

Financial assets	IAS 39 carrying amount 31 December 2017 Shs ' 000	Reclassification Shs ' 000	Remeasurement Shs ' 000	IFRS 9 carrying amount 1 January 2018 Shs ' 000
Amortised cost:				
Balances with Central Bank of Kenya: Opening balance as per IAS 39 and closing balance as per IFRS 9	2,159,276	-	-	2,159,276
Balances with other financial institutions				
Opening balance as per IAS 39	2,495,298	-	-	-
Remeasurement: ECL allowance	-	-	(209)	-
Closing balance as per IFRS 9	-	-	-	2,495,089
Government securities: Opening balance as per IAS 39 and closing balance as per IFRS 9	7,692,403	-	-	7,692,403
Corporate bond investments				
Opening balance as per IAS 39	842,679	-	-	-
Remeasurement: ECL allowance	-	-	(14,593)	-
Closing balance as per IFRS 9	-	-	-	828,086
Customer loans and advances				
Opening balance as per IAS 39	43,471,853	-	-	-
Remeasurement: ECL allowance		-	(577,562)	-
Closing balance as per IFRS 9		-	-	42,894,291
Other investments				
Opening balance as per IAS 39	1,830,097	-	-	-
Remeasurement: ECL allowance	-	-	(2,866)	-
Closing balance as per IFRS 9	-	-	-	1,827,231
Other assets: Opening balance as per IAS 39 and closing balance as per IFRS 9	1,220,179	-	-	1,220,179
Total financial assets measured at amortised cost	**59,711,785**	**-**	**(595,230)**	**59,116,555**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

a) Basis of preparation (continued)

(iii) Changes in accounting policies and disclosures (continued)

The total remeasurement loss of Shs 595,230,000 for Group and Bank was recognised on 1 January 2018 against the related credit exposures.
Revenue reserves' and statutory credit loss adjustments cumulatively amounting to Shs 416,690,000 at Group and Bank levels, being the above adjustments net of deferred tax, were also booked. Refer to the statement of changes in equity for movement

A. Reconciliation of impairment allowance balances from IAS 39 to IFRS 9

The tables below provide reconciliations between the prior period's closing impairment allowances measured in accordance with IAS 39 incurred loss model and to the new impairment allowance measured in accordance with the IFRS 9 expected credit loss model at 1 January 2018.

Group and Bank

Measurement category	Loan loss allowance under IAS 39	Reclassification	Remeasurement	Loan loss allowance under IFRS 9
	Shs ' 000	Shs ' 000	Shs ' 000	Shs ' 000
Loans and receivables (IAS 39) / Financial assets at amortised cost (IFRS 9)				
Cash and balances with financial institutions	-	-	209	209
Loans and advances to customers	2,457,525	-	465,430	2,922,855
Other assets at amortised cost	-	-	2,866	2,866
Investment securities at amortised cost	-	-	14,593	14,593
Held to maturity investments (IAS 39)/ Financial assets at amortised cost (IFRS 9)				
Government and corporate securities	-	-	-	-
Loan commitments, letters of credit and guarantees				
Letters of credit and guarantee contracts			14,502	14,502
Loan commitments	-	-	97,630	97,630
Total	**2,457,525**	**-**	**595,230**	**3,052,655**

The Group has not yet established internal models for measurement of expected credit loss (ECL) on non-loan financial instruments, such as investments securities, interbank balances and other financial assets. However, as at 1 January 2018 and 31 December 2018, the Group estimated the ECL for these financial assets using external default data as proxy and concluded the ECL not to be material for Government securities. As such, no ECL has been recognised on these instruments. The Group will continuously evaluate this in future.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

(B) Consolidation

The consolidated financial statements incorporate the financial statements of the Bank and an entity controlled by the Bank. Control is achieved when the Bank:

- has power over the investee
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns

The Bank reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Bank has less than a majority of the voting rights of an investee, it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally.

The Bank considers all relevant facts and circumstances in assessing whether or not the company's voting rights in an investee are sufficient to give it power over the investee, including:

- the size of the Bank's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Bank, other vote holders or other parties;
- rights arising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Bank has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholder's meetings.

Consolidation of a subsidiary begins when the company obtains control over the subsidiary and ceases when the company loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statement of profit or loss and other comprehensive income from the date the company gains control until the date when the company ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income are attributed to the owners of the company and to the non-controlling interests. Total comprehensive income of subsidiaries is attributed to the owners of the company and to the non-controlling interest even if this results in the non-controlling interests having a deficit balance.

When necessary, adjustments are made to the financial statements for subsidiaries to bring their accounting policies into line with the Group's accounting policies.

All intragroup assets and liabilities, equity, income, expenses and cash flows relating to the transactions between the members of the Group are eliminated in full on consolidation.

Changes in the Group's ownership interests in existing subsidiaries

Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interest and the non- controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to owners of the company.

When the Group loses control of a subsidiary, a gain or loss is recognised in profit or loss and is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and any non-controlling interest. All amounts previously recognised in other comprehensive income in relation to the subsidiary are accounted for as if the Group had directly disposed of the related assets or liabilities of the subsidiary (i.e. reclassified to profit or loss or transferred to another category of equity as specified/permitted by applicable IFRSs). The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under IFRS 39: Financial Instruments: Recognition and Measurement, when applicable, the cost on initial recognition of an investment in an associate or a joint venture.

Refer to note 36 of the financial statements for description of Basis of non- consolidation of an entity under the Group's control.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

(c) Investment in subsidiary

Investment in subsidiary companies are stated at cost less impairment loss where applicable.

(d) Interest income and expense recognition

Interest income and interest expense on interest bearing financial instruments is calculated by applying the effective interest rate to the gross carrying amount, except for:

(i) Purchased or originated credit impaired (POCI) financial assets, for which the original credit-adjusted effective interest rate is applied to the amortised cost of the financial asset; and

(ii) Financial assets that are not "POCI" but have subsequently become credit-impaired, for which interest revenue is calculated by applying the effective interest rate to their amortised cost (i.e.net of the expected credit loss provision) in subsequent reporting periods.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees paid or received that are integral to the effective interest rate, such as origination fees.

(e) Fee and commission income

Fee and commission revenue, including transactional fees, account servicing fees, investment management fees and sales commissions are recognised as the performance obligations under the related services' contracts are met. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. Loan appraisal fees are recognised as revenue when the appraisal has been completed and the Bank has retained no part of the loan package for itself or has retained a part at the same effective interest rate as the other participants.

Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party – such as the arrangement of the acquisition of shares or other securities, or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportionate basis. Performance-linked fees or fee components are recognised when the performance criteria are fulfilled.

(f) Foreign currency translation

(i) Functional and presentation currency

The Group's consolidated financial statements are presented in Kenya Shillings, which is also the Company's Functional and Presentation currency. For each entity in the Group, the Company determines the functional currency and items included in the financial statements of each entity are measured using that Functional currency.

Transactions and balances

Foreign currency transactions that are transactions denominated, or that require 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.

The Group does not have a foreign operation.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

(g) Financial assets and liabilities

The Group adopted IFRS 9 on 1 January 2018. The objective of IFRS 9 is to establish principles that will present relevant and useful information to users of financial statements in relation to:

i) Classification of financial instruments;
ii) Initial and subsequent measurement of financial instruments;
iii) Modification and derecognition of financial instruments; and
iv) Impairment of financial assets.

The Group determines the appropriate classification of its financial assets at initial recognition. It recognises a financial asset in its statement of financial position when it becomes party to the contractual provisions of the instrument.

The Group classifies its financial assets into the following categories:

- financial assets at fair value through profit or loss ("FVTPL");
- financial assets measured at amortised cost; and
- financial assets at fair value through other comprehensive income ("FVTOCI");

Financial assets (except those carried at fair value through profit or loss) are initially recognised in the financial statements at fair value plus transaction costs. Loans and receivables and investments held at amortised cost are carried at amortised cost using the effective interest rate ("EIR") method.

Financial assets at fair value through other comprehensive income and financial assets at fair value through profit or loss are carried at fair value. Gains and losses arising from changes in the fair value of 'financial assets at fair value through profit or loss' are included in profit and loss in the period in which they arise. Gains and losses arising from changes in the fair value of assets at fair value through other comprehensive income are recognised in other comprehensive income and cumulated in a separate reserve in equity until the financial asset is derecognised or impaired, at which time the cumulative gain or loss previously recognised in equity is recognised in profit and loss.

i) Financial assets

Recognition and Subsequent measurement

a) Debt instruments

At initial recognition, the Group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at fair value through profit or loss are expensed in profit or loss.

Except for the Group's financial assets that are designated at initial recognition as at fair value through profit or loss, the Group's financial asset is classified on the basis of both;

- the Group's business model for managing the financial assets; and
- the contractual cash flow characteristics of the financial asset.

Based on these factors, the Group classifies its debt instruments into one of the following three measurement categories:

- Amortised cost: assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest (SPPI), and that are not designated at FVPL, are measured at amortised cost. The carrying amounts of these assets are adjusted by any expected credit loss allowances. Interest income from financial assets is included in "interest and credit related income" using the effective interest rate method.

- Fair value through other comprehensive income (FVOCI): Financial assets that are held for collection of contractual cash flows and for selling, where the assets' cash flows represent SPPI and that are not designated at FVPL, are measured through other comprehensive income (FVOCI). Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses and interest revenue and foreign exchange gains and losses on the instrument's amortised cost which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in "Net gains on disposal of financial instruments". Interest income from the instruments is included in "interest and credit related income" using the effective interest rate.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

g) Financial assets and liabilities (continued)

Financial Assets (continued)

ii) Recognition and subsequent measurement

(a) Debt instruments (continued

Fair value through the profit or loss: Assets that do not meet the criteria for amortised cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognised in profit or loss in the period in which it arises. Interest income and credit related income from these financial assets is included in "interest income" using the effective interest rate method.

Group's business model: The business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of "other" business model and measured at FVPL. Factors considered by the Group in determining the business model for a group of assets include past experience on how cash flows for these assets were collected, how the asset's performance is evaluated and reported by key management personnel, how risks are assessed and managed and how managers are compensated. For example, the liquidity portfolio of assets is held by the Group as part of liquidity management and is generally classified with the hold to collect and sell business model. Securities held for trading are held principally for the purpose of selling in the near term or are part of a portfolio of financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. These securities are classified in the "other" business model and measured at FVPL.

Contractual characteristics of a financial asset / SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Group assesses whether the financial instruments' cash flows represents solely payments of principal and interest (the "SPPI test"). In making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk and a profit margin that is consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

The Group reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. The changes are expected to be very infrequent and none occurred during the year.

b) Equity Instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets e.g. basic ordinary shares.

The Group measures all equity investments at fair value through profit or loss, except where the Group's management has elected, at initial recognition, to irrevocably designate an equity investment at fair value through other comprehensive income. The Group's policy is to designate equity investments as FVOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognised in OCI and are subsequently not reclassified to profit or loss, including on disposal. Impairment losses (and reversals of impairment losses) are not reported separately from other changes in fair values.

Dividends, when representing a return on such investments, continue to be recognised in profit or loss as other income when the Group's right to receive payment is established. Gains and losses on equity investments at FVPL are included in the "Other income" line in the statement of comprehensive income.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

g) Financial assets and liabilities (continued)

Financial Assets (continued)

(ii) Modification of loans

The Group may sometimes renegotiate or otherwise modify the contractual cash flows of loans to customers. When this happens, the Group assesses whether or not the new terms are substantially different to the original terms. The Group does this by considering, among others, the following factors:

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- Whether any substantial new terms are introduced, such as a profit share/equity based return that substantially affects the risk profile of the loan.
- Significant extension of the loan term when the borrower is not in financial difficulty.
- Significant change is interest rate
- Change in the currency of the loan - Insertion of collateral, other security or credit enhancement that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Group derecognises the original financial asset and recognises a "new" asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. Accordingly, the date of the modification is treated as the date of initial recognition of that financial asset when applying the impairment requirements to the modified financial asset. This typically means measuring the loss allowance at an amount equal to 12-month expected credit losses until the criteria for the recognition of lifetime expected credit losses is met.

However, in some unusual circumstances following a modification that results in derecognition of the original financial asset, there may be evidence that the modified financial asset is credit-impaired at initial recognition, and thus, the financial asset is recognised as an originated credit-impaired financial asset. This might occur, for example, in a situation in which there was a substantial modification of a distressed asset that resulted in the derecognition of the original financial asset. In such a case, it may be possible for the modification to result in a new financial asset which is credit- impaired at initial recognition. Differences in the carrying amount are recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, the Group recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate of credit-adjusted effective interest rate for POCI financial assets.

iii) Derecognition other than on a modification

Financial assets, or a portion thereof, are derecognised when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either (i) the Group transfers substantially all the risks and rewards of ownership, or (ii) the Group neither transfers nor retains substantially all the risks and rewards of ownership and the Group has not retained control.

The Group enters into transactions where it retains the contractual rights to receive cash flows from assets but assumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards. These transactions are accounted for as "pass through" transfers that result in derecognition if the Group:

(i) Has no obligation to make payments unless it collects equivalent amounts from the assets;

(ii) Is prohibited from selling or pledging the assets; and

(iii) Has an obligation to remit any cash it collects from assets without material delays.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)
g) Financial assets and liabilities (continued)
Financial Assets (continued)

Collateral (shares and bonds) furnished by the Group under standard repurchase agreements and securities lending and borrowings transactions are not derecognised because the Group retains substantially all the risks and rewards on the basis of predetermined repurchase price, and the criteria for derecognition are therefore not met. This also applies to certain securitisation transactions in which the Group retains a subordinated residual interest.

(iv) Impairment of financial assets

The Group assesses on a forward-looking basis the expected credit losses ("ECL") associated with its debt instrument assets carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.
- Refer to Note 4(a) for further details on how ECLs are determined, including some of the significant underpinning their computation.

h) Financial Liabilities

The Group's holding in financial liabilities represents mainly deposits from banks and customers and other liabilities. Such financial liabilities are initially recognised at fair value and subsequently measured at amortised cost. Financial liabilities are derecognised when they have been redeemed or otherwise extinguished.

The Group's holding in financial liabilities represents mainly customer and bank deposits and other financial liabilities.

(i) Classification and subsequent measurement

Financial liabilities are classified as subsequently measured at amortised cost, except for:

- Financial liabilities at fair value through profit or loss such as derivatives, financial liabilities held for trading (e.g. short positions in the trading booking) and other financial liabilities designated as such at initial recognition. Gains or losses on financial liabilities designated at fair value through profit or loss are presented partially in other comprehensive income (the amount of change in the fair values of the financial liability that is attributable to changes in the credit risk of that liability) and partially profit or loss (the remaining amount of change in the fair value of the liability);
- Financial liabilities arising from the transfer of financial assets which did not qualify for derecognition, whereby a financial liability is recognised for the consideration received for the transfer. In subsequent periods, the Group recognises any expense incurred on the financial liability; and
- Financial guarantee contracts and loan commitments

(ii) Derecognition of financial liabilities

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

(iii) Financial guarantee contracts and loan commitments

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of the debt instrument. Such financial guarantees are given to banks, financial institutions and others on behalf of customers to secure loans, overdrafts and other banking facilities. Financial guarantee contracts are initially measured at fair value and subsequently measured at the higher of:

- The amount of the loss allowance; and
- The premium received on initial recognition less income recognised in accordance with the principles of IFRS 15

Loan commitments provided by the Group are measured as the amount of the loss allowance. The Group has not provided any commitment to provide loans at a below-market interest rate, or that can be settled net in cash or by delivering or issuing another financial instrument, other than for staff facilities. For loan commitments and financial
guarantee contracts, the loss allowance is recognised as a provision. However, for contracts that include both a loan and an undrawn commitment and the Group cannot separately identify the expected credit losses on the undrawn commitment component from those on the loan component, the expected credit losses on the undrawn commitment are recognised together with the loss allowance for the loan to the extent that the combined expected credit losses exceed the gross carrying amount of the loan, the expected credit losses are recognised as provision.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

i) Comparative accounting policies for financial assets and liabilities

The IAS 39 related accounting policies below are provided because financial instruments comparative balances were recognised and measured under this standard.

i) Financial liabilities

The Group's holding in financial liabilities represents mainly deposits from banks and customers and other liabilities. Such financial liabilities are initially recognised at fair value and subsequently measured at amortised cost.

ii) Financial assets

The Group classifies its financial assets into the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity; and available-for-sale financial assets. The directors determine the appropriate classification of its investments at initial recognition.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held-for-trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling or repurchasing it in the short term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorised as held-for-trading unless they are designated and effective as hedging instruments. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative. Where a financial asset contains one or more embedded derivatives that significantly modify financial asset's cash flows, it is accounted for at fair value through profit or loss.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than:

a) Those classified as held-for-trading and those that the Group on initial recognition designates as at fair value through profit or loss;
b) Those that the Group upon initial recognition designates as available-for-sale; or
c) Those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

Loans and receivables are initially recognised at fair value – which is the cash consideration to originate or purchase the loan including any transaction costs – and measured subsequently at amortised cost using the effective interest method.

Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the directors have the positive intention and ability to hold to maturity, other than:

a) Those that the Group upon initial recognition designates as at fair value through profit or loss;
b) Those that the Group designates as available-for-sale; and
c) Those that meet the definition of loans and receivables.

Held-to-maturity investments are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method. Were the Group to sell more than an insignificant amount of held-to-maturity assets, the entire category would be tainted and would have to be reclassified as available-for-sale.

Available-for-sale

Available-for-sale assets are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates, or equity prices or that are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. Financial assets are initially recognised at fair value plus, for all financial assets except those carried at fair value through profit or loss, transaction costs. Financial assets are de-recognised when the rights to receive cash flows from the assets have expired or where the Group has substantially transferred all risks and rewards of ownership.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Significant accounting policies (continued)

i) Comparative accounting policies for financial assets and liabilities (continued)

Financial assets (continued)

iii) Subsequent measurement of financial assets

Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method. Available-for-sale financial assets and financial assets at fair value through profit or loss are carried at fair value. Gains and losses arising from changes in the fair value of 'financial assets at fair value through profit or loss' are included in profit or loss in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised in other comprehensive income and cumulated in a separate reserve in equity until the financial asset is de-recognised or impaired, at which time the cumulative gain or loss previously recognised in equity is recognised in profit or loss. However, interest calculated using the effective interest method is recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in the profit or loss when the Company's right to receive payment is established.

iv) Derecognition of financial assets

Financial assets are de-recognised when the contractual rights to receive the cash flows from these assets have ceased to exist or the assets have been transferred and substantially all the risks and rewards of ownership of the assets are also transferred (that is, if substantially all the risks and rewards have not been transferred, the Group tests control to ensure that continuing involvement on the basis of any retained powers of control does not prevent de-recognition). Financial liabilities are de-recognised when they have been redeemed or otherwise extinguished.

v) Impairment of financial assets

I) Assets at amortised cost

The Group assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after initial recognition of the asset (a "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

(i) significant financial difficulty of the issuer or obligor;
(ii) a breach of contract, such as default or delinquency in interest or principal repayments;
(iii) the Group granting to the borrower, for economic or legal reasons relating to a borrower's financial difficulty, a concession that the Group would not otherwise consider;
(iv) it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
(v) the disappearance of an active market for that financial asset because of financial difficulties; or
(vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

- Adverse changes in the payment status of borrowers in the group; or
- National or local economic conditions that correlate with defaults on the assets in the group.

The Group assesses whether objective evidence of impairment exists individually for financial assets. If there is objective evidence that an impairment loss on loans or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial instrument's original effective interest rate.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

When a loan is uncollectible, it is written off against the related provision for impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised in profit or loss.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Summary of significant accounting policies (continued)

i) Comparative accounting policies for financial assets and liabilities (continued)

vi) Impairment of financial assets (continued)

(i) Assets at amortised cost (continued)

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in profit or loss.

The Group also considers a collective impairment provision for loans not subject to individual assessment, to cover losses which have been incurred but have not yet been identified.

The Group considers evidence of impairment for loans and advances at a collective level. All individually significant financial assets are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortised cost) with similar risk characteristics.

In assessing collective impairment, the Group uses empirical data on 'loss ratios' over the past five years and an emergence period. These are regularly benchmarked against actual outcomes to ensure that they remain appropriate.
Restructured loans, whose terms have been renegotiated are no longer considered to be past due but are treated as new loans after the minimum required number of payments under the new arrangement have been received.

ii) Assets carried at fair value

In the case of financial assets classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the profit or loss.

vi) Reclassification of financial assets

The Group may choose to reclassify a non-derivative financial asset held for trading out of the held-for-trading category if the financial asset is no longer held for the purpose of selling it in the near-term. Financial assets other than loans and receivables are permitted to be reclassified out of the held for trading category only in rare circumstances arising from a single event that is unusual and highly unlikely to recur in the near-term.

In addition, the Group may choose to reclassify financial assets that would meet the definition of loans and receivables out of the held-for-trading or available-for-sale categories if the Group has the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification. Reclassifications are made at fair value as of the reclassification date. Fair value becomes the new cost or amortised cost as applicable, and no reversals of fair value gains or losses recorded before reclassification date are subsequently made.

Effective interest rates for financial assets reclassified to loans and receivables and held-to-maturity categories are determined at the reclassification date. Further increases in estimates of cash flows adjust effective interest rates prospectively. On reclassification of a financial asset out of the 'at fair value through profit or loss' category, all embedded derivatives are re-assessed and, if necessary, separately accounted for.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Summary of significant accounting policies (continued)

i) Borrowings

Borrowings are recognised initially at fair value, generally being their issue proceeds, net of directly attributable transaction costs incurred. Borrowings are subsequently measured at amortised cost and interest is recognised using the effective interest method.

Borrowing costs that relate to qualifying assets, that is, assets that necessarily take a substantial period of time to get ready for their intended use or sale and which are not measured at fair value, are capitalised. All other borrowing costs are recognised in profit or loss. Borrowing costs consist of interest and other costs that an entity incurred in connection with the borrowing of funds

j) Offsetting financial instruments

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

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions.

k) Property and equipment

Property and equipment are stated at cost or as professionally revalued from time to time less accumulated depreciation and any accumulated impairment losses.

Any surplus arising on revaluation is recognised in other comprehensive income and accumulated in the revaluation reserve account. 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.

The Group's policy is to professionally revalue freehold land and buildings at least once every five years. The last valuation was done on 31 December 2016. The valuation considered the highest and best use of the property. The basis of valuation for freehold land and buildings is open market value.

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:

Buildings	2.50%
Fixtures, fittings and equipment	12.50%
ATM Machines	16.70%
Motor vehicles	20%
Computers	20%

Freehold land is not depreciated.

The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period with the effect of any changes in estimate accounted for on a prospective basis.

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.

i) Intangible assets

Intangible assets comprise acquired computer software license costs which are recognised on the basis of expenditure incurred to acquire and bring the specific software to use. These costs are amortised over estimated useful lives of three to ten years.

Costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. During development of these software products, direct costs such as the software development employee costs and an appropriate portion of relevant overheads are recorded as work in progress and amortised from the point at which the asset is ready for use.

Computer software development costs recognised as assets are amortised over an estimated useful life of three to eight years. Costs associated with the maintenance of computer software are expensed as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Summary of significant accounting policies (continued)

(m) Impairment of tangible and intangible assets

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

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a 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 for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

(n) Investment properties

Investment properties comprise land and buildings and parts of buildings held to earn rentals and/or for capital appreciation. Investment properties are measured initially at cost including transaction costs. Subsequent to initial recognition, investment properties are measured at fair value. The fair value, determined annually by external independent valuers. Fair value is based on active market prices as adjusted, if necessary, for any difference in the nature, condition or location of the specific asset.Investment properties are not subject to depreciation. Gains and losses arising from changes in the fair value of investment property are included in profit or loss in the year in which they arise.

Investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from the disposal. Any gain or loss arising on derecognition of the property (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period in which the property is derecognised.

(o) Non-current assets held for sale

The Group classifies a non-current asset as held for sale if, and only if, its carrying amount will be recovered principally through a sale transaction rather than through continuing use. Non-current assets held for sale are measured at the lower of their carrying amounts and fair values less estimated selling costs at end of reporting period date.

Impairment loss arising from any subsequent write-down of the carrying amount of an asset identified for sale to fair value less costs to make the sale is charged to profit or loss in the year in which the loss is identified.

(p) Taxation

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

Current taxation

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

Deferred taxation

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Summary of significant accounting policies (continued)

(p) Taxation (continued

Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences are utilised. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from good will or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit. The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities and assets are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates that have been enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Current and deferred tax for the year

Current and deferred tax are recognised in profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income.

(q) Provisions

A provision is recognised if, as a result of a past event, the group 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.

(r) Contingent liabilities

Provisions for legal claims are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Provisions are not recognised for future operating losses. Provisions are measured at the present value of the expenditure expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation.
Contingent liabilities are possible obligations arising from past events, whose existence will be confirmed only by uncertain future events, or present obligations arising from past events that are not recognised because either an outflow of economic benefits is not probable or the amount of the obligation cannot be reliably measured. Contingent liabilities are not recognised but information about them is disclosed unless the possibility of any outflow of economic benefits in settlement is remote.

(s) Statutory reserve

Further to the credit loss allowances computed in line with international financial reporting standards, the Central Banks have, in their prudential guidelines, specified certain minimum loan loss provisions to be held against various categories of loans and advances. Where credit loss allowances computed in line with the Central Bank regulations exceed those computed on the same loan balances under International financial reporting standards, the excess is recognised as a regulatory loss reserve and is accounted for as an appropriation of retained earnings. The statutory loan loss reserve is non-distributable.

(t) Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessor
Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease.

The Group as lessee
Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

(u) 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 group in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2. Summary of significant accounting policies (continued)

(v) Employee benefit costs

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

The Group and its employees also contribute to the statutory National Social Security Fund (NSSF). 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 Group's contributions in respect of retirement benefit costs are charged to the profit and loss in the period to which they relate.Employee entitlement to leave not taken is charged to profit or loss as it accrues.

(w) Sale and repurchase agreements

Securities sold to the Central Bank of Kenya subject to repurchase agreements ('repos') are retained in the financial statements under government securities and the counterparty liability is included in advances from Central Bank of Kenya. The difference between the sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

(x) Operating segments

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision Maker (Managing Director and CEO). Management then allocates resources to and assesses the performance of the operating segments of the Group.

- Segment result is segment revenue less segment expenses.
- Segment revenue is the revenue that is directly attributable to a segment plus the relevant portion of the Group's revenue that can be allocated to the segment on a reasonable basis.
- Segment expenses are expenses resulting from the operating activities of a segment plus the relevant portion of an expense that can be allocated to the segment on a reasonable basis.
- Segment assets and liabilities comprise those operating assets and liabilities that are directly attributable to the segment or can be allocated to the segment on a reasonable basis.

Capital expenditure represents the total cost incurred during the year to acquire segment assets (property, plant and equipment) that are expected to be used during more than one year.

(y) Comparatives

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

3 Critical accounting estimates and judgements

The preparation of financial statements requires the use of accounting estimates which, by definition, will seldom equal the actual results. The directors also need to exercise judgment in applying the Group's accounting policies.

All estimates and assumptions required in conformity with IFRS are best estimates undertaken in accordance with the applicable standard. Estimates and judgements are evaluated on a continuous basis, and are based on past experience and other factors, including expectations with regard to future events.
This note provides an overview of the areas that involve a higher degree of judgment or complexity, and major sources of estimation uncertainty that have a significant risk of resulting in a material adjustment within the next financial year. Detailed information about each of these estimates and judgements is included in the related notes together with information about the basis of calculation for each affected line item in the financial statements.

a) Measurement of the expected credit loss allowance

The measurement of the expected credit loss allowance for financial assets measured at amortised cost and FVOCI is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 Critical accounting estimates and judgements (continued)

a) Measurement of the expected credit loss allowance (continued)

A number of significant judgements are also required in applying the accounting requirement for measuring ECL, such as:

- Determining criteria for significant increase in credit risk;
- Choosing the appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type
- of product/market and the associated ECL;
- Establishing groups of similar financial assets for the purposes of measuring ECL;
- Determining the relevant period of exposure to credit risk when measuring ECL for credit cards and revolving credit facilities; and
- Determining the appropriate business models and assessing the "solely payments of principal and interest (SPPI)" requirements for financial assets.

4 Financial risk management

The Group defines risk as the possibility of losses being incurred or profits foregone, which may be caused by internal or external factors. The Group aims to achieve an appropriate balance between risk and return and minimise the potential adverse effects of the Group's financial performance.

The most important type of risks to which the Group and the Bank are exposed to are financial risks which include:

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

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established a risk management committee comprising of two non-executive directors to assist in the discharge of this responsibility. The Board has also established the Group Asset and Liability (ALCO), Credit Committee and Risk and Compliance Committees, which are responsible for developing and monitoring risk management policies in their specified areas. With the exception of the ALCO which is a Management Committee, these committees comprise of both non-executive and 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 Group's risk management policies are established to identify and analyse the risks faced by the group, 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 Group, 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.

Financial Risk Management disclosures

The Risk and Compliance Committee is responsible for monitoring compliance with the group's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Group. This committee is assisted in these functions by the Assurance Function. The Assurance Function undertakes reviews of risk management controls and procedures, the results of which are reported to the committee.

4.1 Credit risk- Group and Bank

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises principally from the Group'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 group is also exposed to other credit risks arising from its trading activities including derivatives.

Credit risk is the single largest risk for the Group's business and management carefully manages its exposure to credit risk. For risk management reporting purposes, the Group 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 Financial risk management (continued)
4.1 Credit risk- Group and Bank (continued)

Management of credit risk

The Board of Directors has delegated responsibility for the oversight of credit risk to its credit committee comprising of three non-executive directors and two 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 Group'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 group's risk gradings 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.
- 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 the group 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 group in the management of credit risk.

Credit risk measurement

In measuring credit risk of loans and advances to customers, the Group 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.
- Current exposure on the borrower and the likely future development from which the Group derives the exposure at default.
- Estimated recovery ratio should default occur; this is the amount that can be recovered through sale of collateral.

The Group 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 Group takes into account the customers financial position, past experience and other industry specific factors. The credit risk measurements are embedded in the Group's daily operational management and closely aligned to the Central Bank of Kenya loan classifications. The impairment allowances on loans and advances computed through the Group's internal measures and the Central Bank of Kenya prudential guidelines are contrasted with the measurement of impairment under the IFRS 9.

4.1.1 Loans and advances

The Group and Company align the classification criteria for assets that are past due or impaired in line with regulatory guidelines. In the determination of the classification of accounts, performance is the primary consideration. The classification of an account reflects a judgment about risks of default and loss associated with the credit facility. The classification process establishes a consistent approach to problem recognition, problem labeling, remedial action and the initiation of credit write-offs.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 Financial risk management (continued)
4.1 Credit risk- Group and Bank (continued)
4.1.1 Loans and advances (continued)

Expected credit loss measurement

IFRS 9 outlines a 'three-Stage' model for impairment based on changes in credit quality since initial recognition as summarised below:

- Stage 1: Assets that are performing. If credit risk is low as of the reporting date or the credit risk has not increased significantly since initial recognition, The Group recognises a loss allowance at an amount equal to 12-month expected credit losses. This amount of credit losses is intended to represent lifetime expected credit losses that will result if a default occurs in the 12 months after the reporting date, weighted by the probability of that default occurring.

- Stage 2: Assets that have significant increases in credit risk. In instances where credit risk has increased significantly since initial recognition, the Bank measures a loss allowance at an amount equal to full lifetime expected credit losses. That is, the expected credit losses that result from all possible default events over the life of the financial instrument. For these debt instruments, interest income recognition will be based on the EIR multiplied by the gross carrying amount.

- Stage 3: For debt instruments that have both a significant increase in credit risk plus observable evidence of impairment i.e. have defaulted.

Purchased or originated credit-impaired financial assets are those financial assets that are credit impaired on initial recognition. Their ECL is always measured on a lifetime basis (Stage 3).
A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward looking information.

The following diagram summarises the impairment requirements under IFRS9 (other than purchased or originated credit-impaired financial assets):

Change in credit quality since initial recognition

Stage 1	Stage 2	Stage 3
(Initial recognition)	(Significant increase in credit risk since initial recognition)	(Credit-impaired assets)
12-month expected credit losses	Lifetime expected credit losses	Lifetime expected credit losses

The key judgments and assumptions adopted by the Group in addressing the requirements of the standard are discussed below:

(i) Significant Increase in credit risk (SICR)

The Group's decision on whether to recognize 12-month or lifetime expected credit losses depends on whether there has been a significant increase in credit risk since initial recognition. An assessment of whether credit risk has increased significantly is performed at each reporting date.
When making the assessment, the Group uses the change in the risk of a default occurring over the expected life of the financial instrument instead of the change in the amount of expected credit losses. This forms the basis of stage 1, 2 and 3 classification and subsequent migration.
The Group applies qualitative and quantitative criteria for stage classification and for its forward and backward credit risk migration.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank (continued)

4.1.1 Loans and advances (continued)

(i) Significant Increase in credit risk (SICR) (continued)

Quantitative Criteria

The quantitative criteria is based on relative and not absolute changes in credit quality driven by counterparty ratings and days past due.
The Group considers that financial instruments for which default patterns are not concentrated at a specific point during the expected life of the financial instrument, changes in the risk of a default occurring over the next 12 months may be a reasonable approximation of the changes in the lifetime risk of a default occurring and could be used to determine whether credit risk has increased significantly since initial recognition.
The appropriateness of using changes in the risk of a default occurring over the next 12 months to determine whether lifetime expected credit losses should be recognised depends on the specific facts and circumstances. Risk of default occurring over the next 12 months is not a suitable basis for determining whether credit risk has increased on a financial instrument with a maturity of more than 12 months when:

1. the financial instruments only have significant payment obligations beyond the next 12 months;
2. changes in relevant macroeconomic or other credit-related factors occur that are not adequately reflected in the risk of a default occurring in the next 12 months; or
3. changes in credit-related factors only have an impact on the credit risk of the financial instrument (or have a more pronounced effect) beyond 12 months

The Group's quantitative credit grading, as compared to CBK's prudential guidelines credit grading is as per the table below:

IFRS 9 credit staging / grading	CBK PG/04 Guidelines	Days past due
1	Normal	Up to date and in line with contractual agreements or within 30 days' arrears
2	Watch	31 to 90 days overdue
3	Substandard	91 to 180 days overdue
	Doubtful	181 – 365 days overdue
	Loss	Over 365 overdue

Qualitative Criteria

In addition to the above, the Group considers other qualitative factors in determining the classification above, and may accelerate the classification of credit facilities where deemed appropriate. They include but not limited to:

1. Significant changes in the terms of the same instrument if it were issued at the reporting date that indicate a change in credit risk since initial recognition, e.g.: increase in credit spread; more stringent covenants; increased amounts of collateral or guarantees; or higher income coverage.
2. Significant changes in external market indicators of credit risk for the same financial instrument (or similar instrument of the borrower), e.g.: credit spread; credit default swap prices; length of time or the extent to which the fair value of a financial asset has been less than its amortized cost; other market information related to the borrower, such as changes in the price of a borrower's debt and equity instruments; or external credit rating (actual or expected).
3. Changes in the Group's credit management approach in relation to the financial instrument (e.g. based on emerging indicators of changes in the credit risk of the financial instrument, the Group's credit risk management practice is expected to become more active or focused on managing the instrument, including the instrument becoming more closely monitored or controlled, or the bank specifically intervening with the borrower).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank (continued)

4.1.1 Loans and advances (continued)

(i) Significant Increase in credit risk (SICR) (continued)

4. Actual or expected adverse changes in business, financial or economic conditions significantly affecting borrower's ability to meet its debt obligations (e.g. increase in interest rates or unemployment rates); operating results of the borrower e.g. declining revenues or margins, increasing operating risks, working capital deficiencies, decreasing asset quality, increased balance sheet leverage, liquidity, management problems or changes in the scope of business or organisational structure (such as the discontinuance of a segment of the business) that results in a significant change in the borrower's ability to meet its debt obligations; or regulatory, economic, or technological environment of the borrower that results in a significant change in the borrower's ability to meet its debt obligations (e.g. a decline in the demand for the borrower's sales product because of a shift in technology).
5. Significant changes in the value of collateral or in the quality of third-party guarantees or credit enhancements, which are expected to reduce the borrower's economic incentive to pay or otherwise affect the probability of default; or quality of a guarantee provided by a shareholder (or an individual's parents) if the shareholder (or parents) have an incentive and financial ability to prevent default by capital or cash infusion.
6. Expected changes in the loan documentation (e.g. breach of contract leading to covenant waivers or amendments, interest payment holidays, interest rate step-ups, requiring additional collateral or guarantees).
7. Significant changes in the expected performance and behavior of the borrower, including changes in the payment status of borrowers in the Group (e.g. increase in delayed contractual payments or number of credit card borrowers expected to approach or exceed their credit limit or who are expected to be paying the minimum monthly amount).

(ii) Definition of default and credit-impaired assets

The Group defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

Qualitative criteria

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. These are instances where:

- The borrower is in long-term forbearance
- The borrower is deceased
- The borrower is insolvent or becoming probable that the borrower will enter bankruptcy
- The borrower is in breach of financial covenants
- An active market for that financial asset has disappeared because of financial difficulties
- Concessions have been made by the lender relating to the borrower's financial difficulty
- Financial assets are purchased or originated at a deep discount that reflects the incurred credit losses

The above criteria have been applied to all financial instruments held by the Group and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD) throughout the Group's expected loss calculations.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of six months. This period of six months has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions.

90 day rebuttable presumption

The Group assumes a rebuttable presumption that a default does not occur later than when a financial asset is 90 days past due unless the Group has reasonable and supportable information to demonstrate that a more lagging default criterion is more appropriate.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank

4.1.1 Loans and advances (continued)

(iii) Measuring expected credit loss – inputs, assumptions and estimation techniques (continued)

"ECL" is defined as the amount on a probability-weighted basis as the difference between the cash flows that are due to the Group in accordance with the contractual terms of a financial instrument and the cash flows that the bank expects to receive. ECL is formula driven, i.e. ECL= PD x LGD x EAD (discounted using the EIR)
ECLs are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation, either over the next 12 months (12-month PD) or over the remaining lifetime (Lifetime PD) of the obligation.
- EAD is based on the amounts the Group expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD).
- LGD represents the Group's expectations of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type of seniority of claim and availability of collateral or other credit support. LGD is calculated on a 12-month or lifetime basis, where 12 month LGD is the percentage of loss expected to be made if the default occurs over the next 12 months and lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan. The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

The lifetime PD is developed by applying a maturity profile to the current 12M PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans.

The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and a credit grade. This is supported by a historical analysis.

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type:

- For amortising products or bullet repayment loans, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis. This will also be adjusted for any expected overpayments made by the borrower. Early repayments/refinance assumptions are also incorporated.
- For revolving products, the exposure at default is predicted by taking the current drawn-down balance and adding a "credit conversion factor" which allows for the expected drawdown of the remaining limit by the time of default. These assumptions vary by product type and current limit utilisation band, based on analysis of the Group's recent default data.

The 12-month and lifetime LGDs are determined based on the factors which impact the recoverable amount post default. These vary by product type:

- For secured products, this is primarily based on collateral type and projected collateral values, historical discounts to market/book values due to forced sales, time to repossession and recovery costs observed.
- For unsecured products, LGDs are typically set at product level due to the limited differentiation in recoveries achieved across different borrowers. These LGDs are influenced by collection strategies, including contracted debt sales and prices.

Forward-looking economic information is also included in determining the 12-month and lifetime PD, EAD and LGD. These assumptions vary by the industry segmentation.

The assumptions underlying the ECL calculation – such as how the maturity profile of the PDs and how collateral values change etc. – are monitored and reviewed on an annual basis.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank

4.1.1 Loans and advances (continued)

(iii) Measuring expected credit loss – inputs, assumptions and estimation techniques (continued)

Forward-looking information incorporated in the ECL models

The assessment of SICR and the calculation of ECL both incorporate forward-looking information. The Group has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio. These economic variables and their associated impact on PD, EAD and LGD vary by industry/portfolio segmentation.

Forecasts of the base economic scenario and the possible bearing and bullish scenarios along with scenario weightings are prepared by an expert economic team. The impact of these economic variables on the PD, EAD and LGD is determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

As with any economic forecasts, the projections and likelihoods of occurrence are subject to an inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The Group considers these forecasts to represent its best estimate of the possible outcomes and has analysed the non-linearities and asymmetries within the Group's different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible outcomes.

The key macro-economic factors that were evaluated by the Group and deemed to be most correlated to the historical and forecasted default statistics include interest and foreign exchange rates, Inflation, GDP growth and population statistics.

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political changes, have been considered, but are not deemed to have a material impact on therefore no adjustment has been made to the ECL for such factors. This is reviewed and monitored for appropriateness annually.

Grouping of instruments for losses measured on a collective basis

For expected credit loss provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogenous. In performing this grouping, there must be sufficient information for the group to be statistically credible. In concluding on how to group its exposures, the Group considered its approach to credit risk management and how aspects such as regulatory compliance and internal concentration limits are managed. As such, the Group grouped its loans and advances at amortised cost based on industries such as Manufacturing, Individuals, Finance and Insurance, Building and construction among others.

There were no exposures deemed to be individually significant to merit individual assessment, other than those in Stage 3. The appropriateness of groupings is monitored and reviewed on a periodic basis.

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. Subsequent recoveries of amounts previously written off are recognised as gains in the profit or loss.

The Group 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank

4.1.1 Loans and advances (continued)

Loans and advances at amortised cost less than 30 days past due date are not considered to have experienced SICR, unless other information is available to indicate the contrary. The breakdown of loans and advances based on their staging is summarised below:

Group and Bank	2018				2017
	Stage 1 12 month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total	
Amortised cost	Kes' 000	Kes' 000	Kes' 000	Kes' 000	Kes' 000
Individually impaired / non performing facilities					
Grade 6: Substandard	-	-	902,710	902,710	2,033,078
Grade 7: Doubtful	-	-	5,423,703	5,423,703	4,877,531
Grade 8: Loss	-	-	808,909	808,909	1,449,498
Gross amount	-	-	**7,135,322**	**7,135,322**	**8,360,107**
Provision for expected credit losses	-	-	(1,902,708)	(1,902,708)	(2,358,817)
Carrying amount	-`	-	**5,232,614**	**5,232,614**	**6,001,290**
Collectively impaired					
Grade 1-3: Normal	37,519,796	-	-	37,519,796	35,759,079
Grade 4-5: Watch	-	1,960,361	-	1,960,361	1,810,192
Gross amount	**37,519,796**	**1,960,361**	**-**	**39,480,157**	**37,569,271**
Provision for expected credit losses	(418,310)	(181,368)	-	(599,678)	(98,708)
Carrying amount	**37,101,486**	**1,778,993**	**-**	**38,880,479**	**37,470,563**
Total carrying amount	**37,101,486**	**1,778,993**	**-**	**44,113,093**	**43,471,853**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank

4.1.1 Loans and advances (continued)

Risk limit control and mitigation policies

The Group 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 Group takes security for funds advances and implements guidelines on the acceptability of specific classes of collateral. To minimise credit loss the Group 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 group on behalf of a customer authorising a third party to draw drafts on the group 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 group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

The Group has no significant concentration of credit risk, with exposure spread over a diversity of personal and commercial customers.

Portfolio management is an integral part of the credit risk management process that enables the Group and Company to limit concentrations, reduce volatility, increase liquidity and achieve optimum earnings. The responsibility for portfolio management lies primarily with business units, with oversight and review by credit risk management while the Board Credit Committee is responsible for credit approvals. The Group's portfolio management plan entails:

- The setting up of portfolio targets and concentrations.
- Establishing target market risk acceptance criteria and key success factors. These are subject to regular review to ensure their continued appropriateness.
- Monitoring the portfolio risk profile, risk-adjusted returns, risk concentrations, economic market and competitive data.
- Identifying and analysing trends and concentrations that could affect the risk and performance of the portfolio.
- Stress testing of the portfolio for the purpose of measuring potential losses.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank

4.1.1 Loans and advances (continued)

Maximum exposure to credit risk before collateral held

	Group and Bank			
	2018		2017	
	Sh'000	%	Sh'000	%
Credit exposures				
On – balance sheet items				
Balances with Central Bank of Kenya	2,787,340	5	2,159,276	3
Balances due from other banking institutions	1,222,738	2	2,495,298	4
Government securities	6,946,277	11	7,692,403	12
Loans and advances to customers	44,113,093	72	43,471,853	70
Corporate bonds	392,772	-	842,679	2
Other investments	1,730,698	3	1,830,097	3
Other assets	344,459	-	283,408	1
	57,537,377	**93**	**58,775,014**	**95**
Off-balance sheet items				
Guarantees and letters of credit	4,114,358	7	3,390,281	5
	61,651,735	**100**	**62,165,295**	**100**

The table represents the worst case scenario of credit exposure for 31 December 2018 and 31 December 2017, 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 net carrying amount as reported on the statement of financial position.

Loans and advances to customers comprise of 72% (2017 - 70 %) of the total maximum exposure.

While collateral is an important mitigant to credit risk, the Group's policy is to establish that loans are within the capacity of the customer to repay, as the primary way out. The Group 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk Group and Bank

4.1.1 Loans and advances (continued)

Collateral management

The Bank uses a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is common practice. The acceptability of collateral for credit risk mitigation is guided by the Bank's procedures and policies. The main types of collateral taken are:

Type of lending	Collateral type
Mortgage lending	First ranking legal charge over the property financed.
Personal loans	Check offs and cash backed
Asset finance	Secured by motor vehicles and chattel registrations
Other loans and advances	Debentures over the Company's assets, cash cover in cash margin account, first ranking legal charge over both commercial and residential properties, directors' personal guarantees and Company guarantees.

Valuation of collateral

The Bank has a panel of valuers who undertake valuation of property and other assets to be used as Collateral. The valuers in the panel are qualified professional valuers with adequate experience in the field of property and machinery valuation. Valuation reports on properties are valid for 5 years after which the property and equipment is revalued.

Financial effect of collateral

As at 31 December 2018, 70% (2017: 60%) of the outstanding loan balances were covered by collateral.

Financial instruments subject to offsetting, enforceable master netting arrangements or similar agreements

The Bank holds financial instruments, financial collateral and cash collateral against its loans and advances measured at amortised cost. The Bank is entitled to offset these through enforceable master netting arrangements or similar agreements, in case of default. As at 31 December 2018, no financial assets or financial liabilities had been offset and presented net on the statement of financial position. Cash collateral held as at 31 December 2018 was Shs 438,493,545 (2017: Shs 539,423,182) and this has been included in 'Other liabilities'. No collateral had been pledged for deposits held.

4.1.2 Other non-loan financial assets

ECL on non-loan financial assets such as government securities, other investments at amortised cost and at FVOCI and other financial assets is not measured using the general model. Instead, the Group:

- uses external credit ratings as proxies to infer approximate PDs;
- assumes 100% LGDs
- assigns equal 'loss' and 'no loss' scenarios based on expert judgment;
- EADs are estimated based on the expected maturities of the instruments, most of which are less than 12 months.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.1 Credit risk (continued)

4.1.3 Concentration of risk

Details of significant concentrations of the Group's assets (before impairment), liabilities and off balance sheet items by industry groups are as detailed below:

i) Advances to customers- Group and Bank

	2018		2017	
	Sh'000	%	Sh'000	%
Manufacturing	270,981	1	2,415,192	5
Wholesale and retail	17,386,801	37	16,412,141	36
Transport and communication	3,858,445	8	5,257,380	11
Agriculture	2,669,826	6	2,415,192	5
Business services	404,454	1	522,520	2
Building and construction	3,373,979	7	3,543,792	8
Other	18,650,996	40	15,363,160	33
	46,615,482	**100**	**45,929,378**	**100**
ii) Customer deposits				
Central and local Government	29,620	-	28,520	-
Co-operative societies	343,101	1	334,809	1
Insurance companies	222,436	-	213,714	-
Private enterprises & individuals	47,769,261	99	46,669,578	99
Non-profit institutions	118,771	-	115,509	-
	48,483,189	**100**	**47,362,130**	**100**
iii) Off balance sheet items				
Letters of credit and guarantees	4,114,358	100	3,390,281	100
	4,114,358	**100**	**3,390,281**	**100**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.2 Liquidity risk

4.2.1 Management of liquidity risk

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

The Group'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 Group's reputation.

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. This includes replenishment of funds as they mature or are borrowed by customers.

The Group invests in short term liquid instruments which can easily be sold in the market when the need arises

- The Group enters into lending contracts subject to availability of funds.
- The Group has an aggressive strategy aimed at increasing the customer deposit base.
- The Group 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 group 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 Group are regularly submitted to ALCO.

Exposure to liquidity risk

The key measure used by the Group 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 Group ratio of net liquid assets to deposits from customers at the reporting date and during the reporting period were as follows:

	2018	2017
At 31 December	30.7%	34.6%
Average for the year	33.0%	30.8%
Maximum for the year	36.9%	36.8%
Minimum for the year	29.9%	14.3%

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management objectives and policies (continued)

4.2 Liquidity risk (continued)

4.2.2 Liquidity risk based on undiscounted cash flows- Group

The table below analyses the cash flows payable by the group 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.

31-Dec-18	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1 – 5 years Sh'000	Over 5 years Sh'000	Total Sh'000
Financial assets						
Cash-in hand	3,494,361					3,494,361
Balances with CBK	2,787,339					2,787,339
Balances due from banks	1,222,738					1,222,738
Government securities	11,192	2,011,384	73,216	685,945	4,219,652	7,001,389
Loans and advances	3,176,611	2,006,005	4,480,231	28,988,138	10,473,212	49,124,197
Corporate bonds	-	-	-	460,322	-	460,322
Other investments	-	1,755,232	-	-	-	1,755,232
Other assets	344,459	-	-	-	-	344,459
Total financial assets	**11,036,700**	**5,772,621**	**4,553,447**	**30,134,405**	**14,692,864**	**66,190,037**
Financial liabilities						
Balances due to banks	247,051	-	-	-	-	247,051
Customer deposits	31,395,666	5,227,401	12,370,530	45,373	-	49,038,969
Borrowings	-	-	3,526,693	-	2,361,451	5,888,144
Other liabilities	329,144	-	-	-	-	329,144
Total financial liabilities	**31,971,861**	**5,227,401**	**15,897,223**	**45,373**	**2,361,451**	**55,503,309**
Net liquidity gap	**(20,935,161)**	**545,220**	**(11,343,776)**	**30,089,032**	**12,331,413**	**10,686,728**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

b) Liquidity risk based on undiscounted cash flows- Bank (continued)

31-Dec-18	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1 – 5 years Sh'000	Over 5 years Sh'000	Total Sh'000
Financial assets						
Cash-in hand	3,494,361					3,494,361
Balances with CBK	2,787,339					2,787,339
Balances due from banks	1,222,738					1,222,738
Government securities	11,192	2,011,384	73,216	685,945	4,219,652	7,001,390
Loans and advances	3,176,611	2,006,005	4,480,231	28,988,138	10,473,212	49,124,197
Corporate bonds	-	-	-	460,322	-	460,322
Other investments	-	1,755,232	-	-	-	1,755,232
Other assets	344,459	-	-	-	-	344,459
Total financial assets	**11,036,700**	**5,772,621**	**4,553,447**	**30,134,405**	**14,692,864**	**66,190,037**
Financial liabilities						
Balances due to banks	247,051	-	-	-	-	247,051
Customer deposits	31,522,372	5,227,401	12,370,530	45,373	-	49,165,676
Borrowings	-	-	3,526,693	-	2,361,451	5,888,144
Other liabilities	307,321	-	-	-	-	307,321
Total financial liabilities	**32,076,744**	**5,227,401**	**15,897,223**	**45,373**	**2,361,451**	**55,608,192**
Net liquidity gap	**(21,040,044)**	**545,220**	**(11,343,776)**	**30,089,032**	**12,331,413**	**10,581,845**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

c) Liquidity risk based on undiscounted cash flows- Group

31-Dec-17	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1 – 5 years Sh'000	Over 5 years Sh'000	Total Sh'000
Financial assets						
Cash in hand	3,482,434	-	-	-	-	3,482,434
Balances with CBK	2,159,276	-	-	-	-	2,159,276
Balances due from banks	2,495,298	-	-	-	-	2,495,298
Government securities	10,514	2,941,878	55,412	2,299,974	3,576,389	8,884,167
Loans and advances	6,038,000	722,481	4,218,628	23,860,894	11,089,375	45,929,378
Corporate bonds	-	-	-	1,057,057	-	1,057,057
Other investments	-	1,852,973	-	-	-	1,852,973
Other assets	283,408	-	-	-	-	283,408
Total financial assets	**14,468,930**	**5,517,332**	**4,274,040**	**27,217,925**	**14,665,764**	**66,143,991**
Financial liabilities						
Balances due to banks	201,708	-	-	-	-	201,708
Customer deposits	32,947,279	3,284,754	11,193,076	-	-	47,425,109
Borrowings	-	-	7,743,164	-	2,361,451	10,104,616
Other liabilities	137,470	-	-	-	-	137,470
Total financial liabilities	**33,286,457**	**3,284,754**	**18,936,240**	**-**	**2,361,451**	**57,868,902**
Net liquidity gap	**(18,817,527)**	**2,232,578**	**(14,662,200)**	**27,217,925**	**12,304,313**	**8,275,088**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

c) Liquidity risk based on undiscounted cash flows- Bank

31-Dec-17	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1 – 5 years Sh'000	Over 5 years Sh'000	Total Sh'000
Financial assets						
Cash in hand	3,482,434	-	-	-	-	3,482,434
Balances with CBK	2,159,276	-	-	-	-	2,159,276
Balances due from banks	2,495,298	-	-	-	-	2,495,298
Government securities	10,514	2,941,878	55,412	2,299,974	3,576,389	8,884,167
Loans and advances	6,038,000	722,481	4,218,628	23,860,894	11,089,375	45,929,378
Corporate bonds	-	-	-	1,057,057	-	1,057,057
Other investments	-	1,852,973	-	-	-	1,852,973
Other assets	283,408	-	-	-	-	283,408
Total financial assets	**14,468,930**	**5,517,332**	**4,274,040**	**27,217,925**	**14,665,764**	**66,143,991**
Financial liabilities						
Balances due to banks	201,708	-	-	-	-	201,708
Customer deposits	33,186,279	3,284,754	11,193,076	-	-	47,664,109
Borrowings	-	-	7,743,164	-	2,361,451	10,104,616
Other liabilities	137,470	-	-	-	-	137,470
Total financial liabilities	33,525,457	3,284,754	18,936,240	-	2,361,451	58,107,903
Net liquidity gap	**(19,056,527)**	**2,232,578**	**(14,662,200)**	**27,217,925**	**12,304,313**	**8,036,088**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

c) Liquidity risk based on undiscounted cash flows- Group and Bank (continued)

The following table shows commitments/guarantees and operating lease commitments that are expected to have cash outflows in future from the Group as at 31 December 2018.

		2018 Sh'000	2017 Sh'000
(a)	Letters of credit, guarantees, acceptances	4,114,358	3,390,281
(b)	Operating lease arrangements	5,011,974	4,936,972
(c)	Committed and undrawn facilities	2,018,181	4,230,868
		11,144,513	**12,558,121**

(d) 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 Group separates exposures to market risk into either trading or non-trading portfolios. Trading portfolios include those positions arising from market-making transactions where the Group 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.

Management of market risks

Overall responsibility of managing market risk rests with the 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.

i) 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 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.

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

NOTES TO THE FINANCIAL STATEMENTS (Continued)

d) Market risk (continued)

i) Interest rate risk Group (continued)

31-Dec-18	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1-5 years Sh'000	Over 5 years Sh'000	Non-interest bearing Sh'000	Total Sh'000
Financial assets							
Cash in hand	-	-	-	-	-	3,494,361	3,494,361
Balances with CBK	-	-	-	-	-	2,787,339	2,787,339
Balances due from banks	-	859,843	-	-	-	362,895	1,222,738
Government securities	11,192	2,011,384	73,216	664,852	4,185,632	-	6,946,277
Loans and advances	44,113,093	-	-	-	-	-	44,113,093
Corporate bonds	-	-	-	392,772	-	-	392,772
Other financial assets	-	-	1,733,563	-	-	344,459	2,078,022
	44,124,285	**2,871,227**	**1,806,779**	**1,057,624**	**4,185,632**	**6,989,055**	**61,034,601**
Financial liabilities							
Balances due to banks	247,051	-	-	-	-	-	247,051
Customer deposits	5,227,401	-	7,532,402	45,373	-	35,678,013	48,483,189
Borrowings	-	-	2,862,082	-	2,041,126	-	4,903,207
Other financial Liabilities	-	-	329,144	-	-		329,144
	5,474,452	-	10,723,628	45,373	2,041,126	35,678,013	53,962,592
Interest sensitivity gap	**38,649,833**	**2,871,227**	**(8,916,849)**	**1,012,251**	**2,144,506**	**(28,688,959)**	**7,072,009**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

d) Market risk (continued)

i) Interest rate risk Group (continued)

31-Dec-17	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1-5 years Sh'000	Over 5 years Sh'000	Non-interest bearing Sh'000	Total Sh'000
Financial assets							
Cash in hand	-	-	-	-	-	3,482,434	3,482,434
Balances with CBK	-	-	-	-	-	2,159,276	2,159,276
Balances due from banks	-	1,868,833	-	-	-	626,464	2,495,298
Government securities	10,514	2,941,878	55,412	1,833,525	2,851,075	-	7,692,404
Loans and advances	43,471,853	-	-	-	-	-	43,471,853
Corporate bonds	-	-	-	842,679	-	-	842,679
Other financial assets	-	1,830,097	-	-	-	283,408	2,113,505
	43,482,367	6,640,808	55,412	2,676,204	2,851,075	6,551,582	62,257,448
Financial liabilities							
Balances due to banks	201,708	-	-	-	-	-	201,708
Customer deposits	3,284,754	-	7,294,684	3,898,392	-	32,884,301	47,362,130
Borrowings	-	-	6,330,527	-	2,032,001	-	8,362,529
Other financial liabilities	-	-	-	-	-	391,847	391,847
	3,486,462	-	13,625,211	3,898,392	2,032,001	33,276,148	56,318,214
Interest sensitivity gap	**39,995,905**	**6,640,808**	**(13,569,799)**	**(1,222,188)**	**819,074**	**(26,724,566)**	**5,939,233**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

d) Market risk (continued)

i) Interest rate risk Bank (continued)

31-Dec-18	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1-5 years Sh'000	Over 5 years Sh'000	Non-interest bearing Sh'000	Total Sh'000
Financial assets							
Cash in hand	-	-	-	-	-	3,494,361	3,494,361
Balances with CBK	-	-	-	-	-	2,787,339	2,787,339
Balances due from banks	-	859,843	-	-	-	362,895	1,222,738
Government securities	11,192	2,011,384	73,216	664,852	4,185,632	-	6,946,277
Loans and advances	44,113,093	-	-	-	-	-	44,113,093
Corporate bonds			-	392,772	-	-	392,772
Other financial assets	-	-	1,733,563	-	-	344,459	2,078,022
	44,124,285	**2,871,227**	**1,806,779**	**1,057,624**	**4,185,632**	**6,989,054**	**61,034,601**
Financial liabilities							
Balances due to banks	247,051	-	-	-	-	-	247,051
Customer deposits	5,227,401	-	7,532,402	45,373	-	31,395,666	44,200,841
Borrowings	-	-	2,862,082	-	2,041,126	-	4,903,207
Other financial Liabilities	-	-	307,321	-	-	-	307,321
	5,474,452	-	10,701,805	45,373	2,041,126	31,395,666	49,658,422
Interest sensitivity gap	**38,649,833**	**2,871,227**	**(8,895,026)**	**1,012,251**	**2,144,506**	**(24,406,612)**	**11,376,179**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

d) Market risk (continued)

i) Interest rate risk Bank (continued)

31-Dec-17	Up to 1 month Sh'000	1 – 3 months Sh'000	4 – 12 months Sh'000	1-5 years Sh'000	Over 5 years Sh'000	Non-interest bearing Sh'000	Total Sh'000
Financial assets							
Cash in hand	-	-	-	-	-	3,482,434	3,482,434
Balances with CBK	-	-	-	-	-	2,159,276	2,159,276
Balances due from banks	-	1,868,833	-	-	-	626,464	2,495,298
Government securities	10,514	2,941,878	55,412	1,833,525	2,851,075	-	7,692,404
Loans and advances	43,471,853	-	-	-	-	-	43,471,853
Corporate bonds	-	-	-	842,679	-	-	842,679
Other financial assets	-	1,830,097	-	-	-	283,408	2,113,505
	43,482,367	**6,640,808**	**55,412**	**2,676,204**	**2,851,075**	**6,551,582**	**62,257,448**
Financial liabilities							
Balances due to banks	201,708	-	-	-	-	-	201,708
Customer deposits	3,284,754	-	7,294,684	3,898,392	-	32,884,301	47,362,131
Borrowings	-	-	9,330,527	-	2,032,001	-	11,362,528
Other financial liabilities	-	-	-	-	-	370,058	370,058
	3,486,462	-	16,625,211	3,898,392	2,032,001	33,254,359	59,296,425
Interest sensitivity gap	**39,995,905**	**6,640,808**	**(16,569,799)**	**(1,222,188)**	**819,074**	**(26,702,777)**	**2,961,023**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 Financial risk management (continued)

(d) Market risk-Group and Bank (continued)

(ii) Currency Risk

The Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. 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.

As at 31 December 2018	USD Sh'000	GBP Sh'000	EURO Sh'000	Total Sh'000
Financial assets				
Deposits and balances due from banking institutions	270,621	156,894	98,133	525,648
Financial liabilities				
Borrowings	-	130,371	116,680	247,051
Sensitivity gap	**270,621**	**26,523**	**(18,547)**	**278,597**
	=======	======	=======	=======
As at 31 December 2017				
Financial assets				
Deposits and balances due from banking institutions	352,587	118,597	135,801	606,985
Financial liabilities				
Borrowings	-	139,714	61,994	201,708
Sensitivity gap	**352,587**	**(21,117)**	**73,807**	**405,277**
	=======	======	=======	=======

Market Risks - Sensitivity Analysis

A principal part of the Group'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.
The Group 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 Group uses a combination of scenarios relevant to local businesses and local markets. These scenarios are used to illustrate the effect on the Group's earnings and capital.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 Financial risk management (continued)

(c) Market risks-Group and Bank (continued)

(iii) 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 variable and constant rates.
- The projections make other assumptions including that all positions run to maturity.

Assuming no management actions, a 10%appreciation in interest rates would increase net interest income by Sh 477,267,608 (2017 – Sh 438,000,772), while a 10% depreciation in interest rated would decrease net interest income by Sh 477,267,608 (2017 – Sh 438,000,772).

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 net currency positions are highly effective.
- The Base currency in which the Group's business is transacted is Kenya Shillings.

Assuming no management actions, a 10% parallel appreciation in all foreign currencies would increase earnings by Sh 33,745,556 (2017 - Sh 28,876,133), while a 10% parallel appreciation in all foreign currencies would decrease net interest income by Sh 33,745,556 (2017 - Sh 28,876,133).

Capital Management

Regulatory capital

The Group's objectives when managing capital are:

- To safeguard the Group's 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 developments.
- 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 Shs 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 8 % of total deposit liabilities
d) Maintain total capital of not less than 14.5% of risk weighted assets plus risk weighted off balance sheet items.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 Financial risk management (continued)

Capital management (continued)

Regulatory capital (continued)

The Insurance Regulatory Authority requires Family Insurance Agency to maintain a minimum level of regulatory capital of Shs 1,000,000. The agency has complied with the capital requirement.

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business.

The impact of the level of capital on shareholders' return is also recognised and the Group recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

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

The Group and its individually regulated operations have complied with all externally imposed capital requirements throughout the year.

Fair Value of financial assets and liabilities

IFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1).
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2).
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) level 3

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management (continued)
Fair value of financial assets and liabilities

Group	Level 1 Shs'000	Level 2 Shs'000	Level 3 Shs'000	Fair value Shs'000	Carrying value Shs'000
At 31 December 2018					
Assets					
Cash and balances with CBK	6,281,701	-	-	6,281,701	6,281,701
Balances due from banking institutions	-	-	1,222,738	1,222,738	1,222,738
Loans and advances to customers	-	-	40,016,317	40,016,317	44,113,093
Government securities at amortised cost	4,013,678	-	104,113	4,117,791	6,946,277
Other investment	-	-	1,738,742	1,738,742	1,738,698
Other financial assets	-	-	344,459	344,459	344,459
	10,295,379	**-**	**43,426,369**	**53,721,748**	**60,646,966**
Liabilities					
Deposits from customers	-	-	48,558,691	48,558,691	48,483,189
Borrowings	-	-	3,571,251	3,571,251	4,903,207
Other financial liabilities			329,144	329,144	329,144
	-	**-**	**52,459,086**	**52,459,086**	**53,715,540**

	Level 1 Shs'000	Level 2 Shs'000	Level 3 Shs'000	Fair value Shs'000	Carrying value Shs'000
At 31 December 2017					
Assets					
Cash and balances with CBK	5,641,710	-	-	5,641,710	5,641,710
Balances due from banking institutions	-	-	2,495,298	2,495,298	2,495,298
Loans and advances to customers	-	-	41,195,697	41,195,697	43,471,853
Financial assets – held-to-maturity	4,213,913	-	3,007,804	7,221,717	7,692,403
Other investments	-	-	-	1,830,097	1,830,097
Other financial assets	-	-	283,408	283,408	283,408
	9,855,623	**-**	**48,812,304**	**58,667,927**	**61,414,769**
Liabilities					
Deposits from customers	-	-	47,362,131	47,362,131	47,362,131
Borrowings	-	-	6,214,990	6,214,990	8,362,529
Other financial liabilities	-	-	479,639	479,639	479,639
	-	**-**	**54,056,760**	**54,056,760**	**56,204,299**

The fair values of the other financial assets and liabilities held by the Group approximate the respective carrying amounts, due to the generally short periods to contractual re-pricing or maturity dates as set out in the previous maturity analysis.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management (continued)
Fair value of financial assets and liabilities (continued)

Bank	Level 1	Level 2	Level 3	Fair value	Carrying value
	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000
At 31 December 2018					
Assets					
Cash and balances with CBK	6,281,701	-	-	6,281,701	6,281,701
Balances due from banking institutions	-	-	1,222,738	1,222,738	1,222,738
Loans and advances to customers	-	-	40,016,317	40,016,317	44,113,093
Government securities at amortised cost	4,013,678		104,113	4,117,791	6,946,277
Other investment	-	-	1,738,742	1,738,742	1,733,563
Other financial assets			344,459	344,459	344,459
	10,295,379	**-**	**43,426,369**	**53,721,748**	**60,641,831**
Liabilities					
Deposits from customers	-	-	48,558,691	48,558,691	48,558,691
Borrowings	-	-	3,571,251	3,571,251	4,903,207
Other financial liabilities			685,781	685,781	685,781
	-	**-**	**52,815,723**	**52,815,723**	**54,147,679**

	Level 1	Level 2	Level 3	Fair value	Carrying value
	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000
At 31 December 2017					
Assets					
Cash and balances with CBK	5,641,710	-	-	5,641,710	5,641,710
Balances due from banking institutions	-	-	2,495,298	2,495,298	2,495,298
Loans and advances to customers	-	-	41,195,697	41,195,697	43,471,853
Financial assets – held-to-maturity	4,213,913	-	3,007,804	7,221,717	7,692,403
Other investments	-	-	1,835,284	1,835,284	1,830,097
Other financial assets	-	-	479,639	479,639	479,639
	9,855,623	**-**	**49,013,722**	**58,869,345**	**61,611,000**
Liabilities					
Deposits from customers	-	-	47,362,131	47,362,131	47,725,108
Borrowings	-	-	6,214,990	6,214,990	8,362,529
Other financial liabilities			479,639	479,639	479,639
	-	**-**	**54,056,760**	**54,056,760**	**56,567,276**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. Financial risk management (continued)

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

	2018 Sh'000	2017 Sh'000
Tier 1 capital		
Share capital	1,287,108	1,287,108
Share premium	5,874,661	5,874,661
Retained earnings	4,072,054	3,957,973
Total Tier 1 capital	**11,233,828**	**11,119,742**
Tier 2 capital		
Revaluation reserves (25%)	48,156	48,156
Term subordinated debt	2,018,800	2,018,800
General loan loss provision (statutory reserve)	-	295,929
Total Tier 2 capital	2,066,956	2,362,885
Total regulatory capital	**13,300,780**	**13,482,627**
Risk-weighted assets	**65,186,401**	**66,207,095**
Capital ratios		
Total regulatory capital expressed as a percentage of total risk-weighted assets (CBK minimum 14.5%)	20.33%	19.86%
Total tier 1 capital expressed as a percentage of risk-weighted assets (CBK minimum 10.5%)	17.23%	16.36%

NOTES TO THE FINANCIAL STATEMENTS (Continued)

	Group		Bank	
	2018	2017 Restated	2018	2017 Restated
6. Interest income	Sh'000	Sh'000	Sh'000	Sh'000
Interest on loans and advances	6,101,256	6,637,550	6,101,256	6,637,550
Interest on bank placements	84,848	38,880	84,848	38,880
Interest on amortised cost (HTM)assets:				
- government securities	772,110	778,517	772,110	778,517
- corporate bonds and commercial paper	98,376	105,975	98,376	105,975
	7,056,590	7,560,922	7,056,590	7,560,922
7. Interest expense				
Interest on customer deposits	1,508,297	1,578,034	1,514,102	1,584,270
Interest on balances due to banks	26,058	101,140	26,058	101,140
Interest on borrowings	749,559	988,708	749,559	988,708
	2,283,914	2,667,882	2,289,719	2,674,118
8. Fees, commission and other income				
(a) Fee and commission income				
Transaction related fees	1,705,062	1,509,492	1,705,062	1,509,492
Credit related fees and commissions	125,800	108,907	125,800	108,907
Ledger related fees and commissions	207,352	161,545	207,352	161,545
	2,038,214	1,779,944	2,038,213	1,779,944
(b) Other Income				
Brokerage commissions	64,282	71,363	-	-
Other incomes	59,021	33,134	59,021	33,134
	123,303	104,497	59,021	33,134

NOTES TO THE FINANCIAL STATEMENTS (Continued)

9 Operating expenses

	Group		Bank	
	2018	2017	2018	2017
	Sh'000	Sh'000	Sh'000	Sh'000
Staff costs (Note 10)	1,860,030	2,339,512	1,814,095	2,290,569
Directors' emoluments - Fees	66,490	70,089	63,670	66,020
- Other	7,545	4,388	7,545	4,388
Depreciation – property and equipment (note 22)	636,986	754,055	634,705	755,773
Amortisation of intangible assets (note 23)	126,825	143,176	124,896	141,448
Contribution to Deposit Protection Fund	70,990	83,044	70,990	83,044
Auditors' remuneration	14,819	11,704	14,173	11,182
Amortisation of prepaid operating lease	4,850	4,623	4,850	4,623
Marketing expenses	116,638	153,260	116,623	151,998
Occupancy expenses	1,036,120	1,191,196	1,035,292	1,189,363
Other operating expenses	1,691,140	2,224,371	1,690,569	2,216,614
	5,632,443	6,979,418	5,577,408	6,915,021

10 Staff costs

Salaries and wages	1,571,489	1,958,113	1,531,295	1,916,669
Training, recruitment and staff welfare costs	57,523	96,261	57,764	96,261
Contributions to defined contribution pension scheme	101,972	119,884	100,365	118,184
Medical expenses	134,237	165,249	130,199	160,237
Leave pay provision movement	(8,179)	(3,458)	(8,422)	(4,137)
NSSF contributions	2,988	3,463	2,894	3,355
	1,860,030	2,339,512	1,814,095	2,290,569

NOTES TO THE FINANCIAL STATEMENTS (Continued)

11 Taxation

	Group		Bank	
	2018	2017	2018	2017
	Sh'000	Sh'000	Sh'000	Sh'000
Taxation				
a)Taxation charge				
Current tax based on the taxable profit at 30% (2017: 30%)	214,022	6,521	209,259	1,762
Deferred tax credit (note 29)	(23,840)	(349,723)	(24,225)	(349,378)
Overprovision of current tax in prior years	534	(13,648)	-	(13,648)
Total charge/ (credit)	190,716	(356,850)	185,034	(361,264)
b) Reconciliation of accounting profit to tax charge				
Profit /(loss) before taxation	434,932	(1,357,638)	419,880	(1,370,841)
Tax calculated at a tax rate of 30% (2017: 30%)	130,288	(407,291)	125,964	(411,252)
Tax effect of expenses not deductible for tax purposes	(37,211)	100,986	(36,673)	100,725
Tax effect of income not taxable	97,105	(36,897)	95,744	(37,089)
Overprovision of current tax in prior years	534	(13,648)	-	(13,648)
	190,716	(356,850)	185,034	(361,264)
c) Corporate tax recoverable				
At beginning of the year	(788,944)	(776,826)	(755,013)	(738,137)
Charge for the year	214,022	6,521	209,259	1,762
Overprovision of current tax in prior years	534	(13,648)	-	(13,648)
Tax paid during the year	(12,707)	(4,991)	(6,093)	(4,991)
At end of the year	(587,095)	(788,944)	(551,846)	(755,013)

NOTES TO THE FINANCIAL STATEMENTS (Continued)

12 Earnings per share – Group & Bank

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

	Group		Bank	
	2018	2017	2018	2017
Profit / (loss) (Sh'000)	244,216	(999,781)	234,816	(1,008,568)
Weighted average number of shares during the year (000)	1,245,187	1,245,187	1,245,187	1,245,187
Earnings per share:				
Basic and diluted (Sh)	0.20	(0.80)	0.19	(0.81)

There were no potential dilutive shares outstanding at 31 December 2018.

13 Cash and cash balances with Central Bank of Kenya – Group & Bank

	2018 Sh'000	2017 Sh'000
Cash in hand	3,494,361	3,482,434
Balances with Central Bank of Kenya - cash ratio & other balances	2,787,340	2,159,276
	6,281,701	5,641,710

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 2018, the cash ratio reserve requirement was 5.25% (2017 – 5.25%) of all customer deposits held by the Bank. These funds are not available to finance the Bank's day to day operations.

14 Balances due from banking institutions – Group & Bank

	2018 Sh'000	2017 Sh'000
a) Balances due from banking institutions maturing within 90 days:		
Overnight lending and placement with other banks	863,059	1,868,833
Balances due from local banking institutions	1,319	1,319
Balances due from foreign banking institutions	358,569	625,145
ECL on interbanks	(209)	-
	1,222,738	2,495,298
b) Balances due to banking institutions maturing within 90 days:		
Balances with local banking institutions	247,051	201,708

Deposits with/from local banks as at 31 December 2018 represent overnight lending.

The effective interest rate on deposits due from local banking institutions at 31 December 2018 was 4.55% (2017 –8.61 %).

The effective interest rate on deposits due to local banking institutions at 31 December 2018 was 2.77% (2017 –7.89 %).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

15 Government Securities

	Group		Bank	
	2018 Sh'000	2017 Sh'000	2018 Sh'000	2017 Sh'000
Treasury bonds – at amortised cost (2017: Held to maturity)	4,988,617	4,772,704	4,988,617	4,772,704
Treasury bills at amortised cost (2017:Held to maturity)	1,957,660	2,919,699	1,957,660	2,919,699
	6,946,277	7,692,403	6,946,277	7,692,403
The maturity profile of government securities is as follows:				
Maturing within one year	2,061,773	3,007,804	2,061,773	3,007,804
Maturing between 2 to 5 years	-	1,833,525	-	1,833,525
Maturing after 5 years	4,884,504	2,851,074	4,884,504	2,851,074
	6,946,277	7,692,403	6,946,277	7,692,403

The weighted average effective interest rate on treasury bonds at 31 December 2018 was 9.257%, (2017 -10.66 %). The weighted average effective interest rate on treasury bills was 10.43% (2017-11.02%).

As of 31 December 2018, no treasury bonds were pledged as collateral under repurchase agreements with the Central Bank of Kenya, (2017: Nil)

16 Loans and advances to customers- Group & Bank

a) Net carrying value of loans

	Group and Bank	
	2018 Shs 000	2017 Shs 000
Term Loans	44,211,340	43,557,011
Overdrafts	2,370,287	2,347,930
Credit Cards	33,855	24,436
Total	46,615,482	45,929,378
Impairment for expected credit losses	(2,502,389)	(2,457,525)
Net loans and advances at amortised cost	44,113,093	43,471,853

b) Analysis of gross loans and advances by maturity

Maturing:		
Within one year	10,971,565	10,246,677
One year to three years	12,564,052	13,080,890
Over 3 years	23,079,865	22,601,810
	46,615,482	45,929,378

NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Loans and advances to customers- Group & Bank (continued)

	Group and Bank	
	2018	2017 (Restated)
	Shs 000	Shs 000
C) Credit impairment charges		
Stage 1	(115,776)	360,685
Stage 2	40,543	54,306
Stage 3	2,529,184	1,029,472
Write back / recoveries	(1,249,678)	-
	(1,204,273)	1,444,462

Significant changes in the gross carrying amounts of loans and advances to customers that contributed to movements in loss allowances were new loans advanced in the year, as well as write off of impaired loans.
The table below shows the movement in gross loans and advances between the various credit quality stages in the year.

The table below shows the movement in gross loans and advances between the various credit quality stages in the year.

	12-month ECL	Lifetime ECL	Lifetime ECL	Total
	SHS 000	SHS 000	SHS 000	SHS 000
Loans and advances to customers at amortised cost				
Gross carrying amount as at 01 January 2018	35,759,078	1,810,192	8,360,108	45,929,378
Changes in the gross carrying amount				
Transfer to stage 1	791,983	(422,273)	(369,710)	-
Transfer to stage 2	(647,913)	704,875	(56,962)	-
Transfer to stage 3	(280,336)	(513,479)	793,815	-
Net new financial assets originated or purchased	1,009,655	1,203,000	3,651	2,216,306
Foreign exchange and other changes	887,689	(821,438)	(352,318)	(286,067)
Write-offs	(358)	(516)	(1,243,261)	(1,244,135)
Gross carrying amount as at 31 December 2018	37,519,798	1,960,361	7,135,323	46,615,482

c) Impairment of financial assets

The loss allowance recognised in the period is impacted by a variety of factors as follows:

- Transfers between Stage 1 and Stage 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit impaired in the period, and the consequent "step up" or "step down" between 12-month and lifetime ECL;
- Additional allowance for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period;
  Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Loans and advances to customers- Group & Bank (continued)

The following tables provide details of the changes in the loss allowance in the year due to these factors:

Group and Bank	Stage 1	Stage 2	Stage 3	
Loss allowance on Loans and advances to customers at amortised cost	12-month ECL	Lifetime ECL	Lifetime ECL	Total
	Shs 000	Shs 000	Shs 000	Shs 000
At start of year	44,402	54,306	2,358,817	2,457,525
- Impact of initial application of IFRS 9	489,740	87,722	-	577,462
	534,142	142,028	2,358,817	3,034,987
Changes in the loss allowance				
Transfer to stage 1	139,452	(54,095)	(85,357)	-
Transfer to stage 2	(10,805)	52,999	(42,194)	-
Transfer to stage 3	(319,189)	(452,300)	771,489	-
New financial assets originated or purchased	100,075	431,045	327,058	858,178
Changes in models/risk parameters	(15,851)	9,499	148,504	142,152
Foreign exchange and other movements	(9,458)	53,396	160,005	203,943
Total charge	(115,776)	40,543	1,279,505	1,204,272
Write-offs	(55)	(1,201)	(1,735,614)	(1,736,870)
At 31 December 2018	418,311	181,371	1,902,708	2,502,390
	======	======	=========	=========

The weighted average effective interest rate on advances to customers at 31 December 2018 was 12.19% (2017 – 12.19 %). Included in gross advances of Sh 46,521,203,000 (2017: Sh 45,929,378,000) are loans and advances amounting to Sh 7,135,321,000 (2017: Sh 8,360,108,000) which have been classified as non-performing (impaired).

The related party transactions and balances are covered under Note 35 and concentration of advances to customers is covered under Note 4.

17 Corporate bonds at amortised cost (2017: Held to maturity) Group & Bank

	2018 Sh'000	2017 Sh'000
At amortised cost:		
Britam Holdings Limited	-	425,403
Centum Limited	407,364	417,276
ECL on amortised cost bonds	(14,592)	-
	392,772	842,679
	=====	=====
The maturity profile of corporate bonds is as follows:		
Within 1 year	-	-
Maturing 1 to 5 years	392,772	842,679
Maturing after 5 years	-	-
	392,772	842,679
	=====	=====

The weighted average effective interest rate on corporate bonds as at 31 December 2018 was 13% (2017 – 13.00 %).The Britam Holdings corporate bond was redeemed during the year.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Other assets

	Group		Bank	
	2018	2017	2018	2017
	Sh'000	Sh'000	Sh'000	Sh'000
Un-cleared items in the course of collection	221,613	160,562	221,613	160,562
Prepayments	152,771	393,653	152,771	393,653
Deposits for services	117,932	134,316	117,932	134,316
Discount on corporate bonds	122,846	122,846	122,846	122,846
Others	992,676	975,284	952,508	936,771
	1,607,838	1,786,661	1,567,670	1,748,148

All other assets are current.

19 Other investments

	Bank and Group	
	2018	2017
	Sh'000	Sh'000
Principal balance	1,907,773	1,909,097
Accrued interest	4,789	-
Provision for expected loss	(181,865)	(79,000)
	1,730,698	1,830,097

20 Investment in subsidiary- BanK

			2018	2017
	No of shares	Holding	Sh'000	Sh'000
Family Insurance Agency Limited	1,000	100%	1,000	1,000

The subsidiary is a wholly owned Limited Liability Company incorporated and domiciled in Kenya. The company was previous named Dhamana Insurance Agency Limited and was incorporated on 22 May 2015. The company received its licence to operate Insurance Agency/brokerage business on 30 December 2010 and started trading in 2010. Subsequently, the subsidiary acquired Family Insurance Brokers Limited on 31 July 2015 and changed its name to Family Insurance Agency Limited.

The principal activity of the company is that of an insurance agency business.
Investment in subsidiary is non-current.

21 Investment properties - Group & Bank

At start and end of year	18,200	18,200

Investment property relates to Leasehold land acquired at a cost of Shs 24,500,000 as part of the Group's expansion plans and Leasehold land acquired at a cost of Shs 3,170,000 for national customer promotion raffle in 2015. Part of the land at value of Shs 7,200,000 was given out in the "Kunacha Mili na Acre," promotion to the various winners.
Investment properties is non-current.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and Equipment- Group

	Freehold Land	Buildings	Leasehold improvements	Computer	Motor vehicles	Fixtures, fittings and equipment	Total
Cost/ Valuation	Sh'000	Sh'000	Sh'000	Sh'000	Sh'000	Sh'000	Sh'000
Year ended 31 December 2017							
At 1 January 2017	569,001	443,948	2,914,707	2,127,959	171,521	1,235,884	7,463,019
Additions	-	-	75,505	16,269	-	128,426	220,200
Gain on revaluation	-	-	-	-	(54,701)	-	(54,701)
At 31 December 2017	569,001	443,948	2,990,212	2,144,228	116,820	1,364,310	7,628,518
Depreciation							
At 1 January 2017	-	44,196	1,330,703	1,319,710	97,718	502,846	3,295,174
Charge for the year	-	11,099	273,295	312,742	23,977	136,941	758,055
Disposal		-	-	-	(47,297)		(47,297)
At 31 December 2017	-	55,295	1,603,998	1,632,452	74,398	639,787	4,005,391
Net Book Value							
At 31 December 2017	569,001	388,653	1,386,214	511,776	42,421	724,523	3,622,587
Year ended 31 December 2018							
At 1 January 2018	569,001	443,948	2,990,212	2,144,228	116,820	1,364,310	7,628,519
Additions	-	-	13,351	10,721	-	4,340	28,412
Disposal							
Write offs	-	-	(266,043)	-	-	-	(266,043)
At 31 December 2018	569,001	443,948	2,737,520	2,154,949	116,820	1,368,650	7,390,888
Depreciation							
At 1 January 2018	-	55,295	1,603,998	1,632,453	74,398	639,787	4,005,931
Charge for the year	-	11,099	268,478	205,214	18,910	133,284	636,986
Disposal	-	-	(93,802)		-	-	(93,802)
At 31 December 2018	-	66,394	1,778,676	1,837,667	93,308	773,071	4,549,115
Net book value							
At 31 December 2018	569,001	377,555	958,846	317,280	23,512	595,579	2,841,773

NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and Equipment- Bank

	Freehold land	Buildings	Leasehold improvements	Computer	Motor vehicles	Fixtures, fittings and Equipment	Total
Cost/ Valuation	Sh'000	Sh'000	Sh'000	Sh'000	Sh'000	Sh'000	Sh'000
Year ended 31 December 2017							
At 1 January 2017	569,001	443,948	2,911,121	2,123,557	166,627	1,234,929	7,449,184
Additions	-	-	75,206	15,738		127,762	218,706
Disposal	-	-	-	-	(53,218)	-	(53,218)
At 31 December 2017	569,001	443,948	2,986,327	2,139,295	113,409	1,362,691	7,614,672
Comprising:							
At cost	499,913	32,288	2,986,327	2,139,295	117,024	1,359,076	7,133,924
At valuation	69,088	411,660					480,748
At 31 December 2017	569,001	443,948	2,986,327	2,139,295	117,024	1,359,076	7,614,672
Depreciation							
At 1 January 2017	-	35,221	1,339,313	1,317,843	95,415	502,425	3,290,216
Charge for the year	-	11,099	273,295	311,877	23,176	136,326	755,773
Disposal	-	-	-		(47,102)	-	(47,102)
At 31 December 2017	-	46,320	1,612,607	1,629,720	71,489	638,751	3,998,887
Net book value							
At 31 December 2017	569,001	397,628	1,373,719	509,575	45,535	720,324	3,615,785
Year ended 31 December 2018							
At 1 January 2018	569,001	443,948	2,986,327	2,139,295	117,024	1,359,093	7,614,672
Additions	-	-	13,351	10,723	-	4,340	28,412
Disposal	-	-	(265,897)	-	-	-	(265,897)
At 31 December 2018	569,001	443,948	2,733,781	2,150,018	117,024	1,363,432	7,377,205
Comprising:							
At cost	499,913	32,288	2,733,781	2,150,018	117,024	1,363,432	6,896,456
At valuation	69,088	411,660	-	-	-	-	480,748
At 31 December 2018	569,001	443,948	2,733,781	2,150,018	117,024	1,363,432	7,377,205
Depreciation							
At 1 January 2018	-	46,320	1,612,608	1,629,719	71,489	638,751	3,998,887
Charge for the year	-	11,099	267,992	204,350	18,108	133,156	634,705
Disposal	-		(93,802)	-	-	-	(93,802)
At 31 December 2018	-	57,418	1,786,880	1,834,069	89,597	771,907	4,539,872
Net book value							
At 31 December 2018	569,001	386,529	946,901	315,949	27,427	591,525	2,837,332

NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and Equipment- Bank (continued)

The land and buildings were re-valued as at 30 June 2016 by Ebony Estate Valuers Limited, Registered Valuers who are independent of the Group. Valuations for the properties were made on the basis of the open market value. In accordance with IFRS 13, the fair value ranking of the freehold 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.

23 Intangible assets - Computer software

	Group		Bank	
	2018 Sh'000	2017 Sh'000	2018 Sh'000	2017 Sh'000
Cost				
At 1 January	1,244,032	1,081,090	1,235,313	1,073,809
Additions	19,678	165,079	19,679	163,642
WIP	233,952	(2,137)	215,015	(2,138)
At 31 December	1,497,662	1,244,032	1,470,007	1,235,313
Amortisation				
At 1 January	773,145	629,969	769,786	628,338
Charge for the year	126,825	143,176	124,897	141,449
At 31 December	899,970	773,145	894,684	769,787
Net book value				
At 31 December	597,692	470,887	575,323	465,526

24 Prepaid Operating Lease Rentals- Group & Bank

	2018 Sh'000	2017 Sh'000
Leasehold land:		
Cost		
At 1 January and 31 December	180,335	180,335
Amortisation		
At 1 January	31,599	26,978
Charge for the year	4,851	4,621
At 31 December	36,450	31,599
Net book value		
At 31 December	143,885	148,736

NOTES TO THE FINANCIAL STATEMENTS (Continued)

25 Customer deposits

	Group		Bank	
	2018	2017	2018	2017
	Sh'000	Sh'000	Sh'000	Sh'000
Customer deposits				
Current and demand accounts	31,393,508	30,458,091	31,395,562	30,467,069
Savings accounts	3,127,000	2,964,292	3,127,000	2,964,292
Fixed deposit accounts	13,962,681	13,939,747	14,036,129	13,993,747
	48,483,189	47,362,130	48,558,691	47,425,108
Maturity analysis of customer deposits				
Repayable:				
On demand	31,393,508	30,458,091	31,395,666	30,467,069
Within one year	17,050,894	16,904,039	17,124,238	16,958,039
1-5 years	38,787	-	38,787	-
	48,483,189	47,362,130	48,558,691	47,425,108

The weighted average effective interest rate on interest bearing customer deposits at 31 December 2018 was 8.49 % (2017 – 10.39% The related party transactions and balances are covered under note 35 and concentration of customers' deposits is covered under note 4.

26 Borrowings - Group & Bank

	2018	2017
	Sh'000	Sh'000
a) Analysis		
European Investment Bank (EIB)	2,340,088	5,633,628
OIKO Credit	507,978	677,684
Waste Finish Ink	10,864	10,864
Water Credit Alternative Channels	3,152	8,351
	2,862,082	6,330,527
Corporate Bond	2,070,653	2,074,768
Unamortised origination fees	(29,528)	(42,766)
	4,903,207	8,362,529
b) Movement:		
At beginning of the year	8,362,528	8,933,191
Received in the year	2,211	7,931
Accrued interest	162,227	319,452
Repaid in the year	(3,623,759)	(898,045)
At end of the year	4,903,207	8,362,529

NOTES TO THE FINANCIAL STATEMENTS (Continued)

26 Borrowings - Group & Bank (continued)

EIB loan is a long term, unsecured floating rate and fixed rate facility which is denominated in EURO, USD and KES. The EURO and USD loans are repayable within 5 years while the KES loans are repayable within 7 years. The interest rate charged for a non KES tranche is based on margin of 1.85%. The loan is a long term facility repayable in 6.5 years. The interest rate charged is 9.78% p.a. The loan repayments are due on the 10 of July and 10 of January of every year. The repayments of the principal commenced 10 July 2016.
For the KES Tranche a margin per annum fixed for the life of the relevant tranche, equal to 1.85% plus a currency risk premium determined in accordance with the following table is charged.

Tenor of the Tranche (years)	Currency risk premium p.a
4 years	5.50%
5 years	6.00%
6 years	6.50%
7 years	7.00%

The OIKO loan is credit from OIKO Credit for the purpose of targeting financial intervention in sanitation and hygiene. The interest charged is 10.10 % (2017: 11.47%) on a reducing balance basis as is will be repaid in 6 annual instalments of Shs 166,666,667.

Waste Finish Ink Loan is a fund delegated to Family Bank Limited by Finish Ink for the funding of various sanitation projects in Kenya. Family Bank Limited does not pay any interest on these funds. Expenses incurred in respect to this fund are offset off the fund amount.

The Water Credit Alternative Channels loan is a fund delegated to Family Bank Limited by Water.org for the funding of various sanitation projects in Kenya. Family Bank Limited does not pay any interest on these funds. Expenses incurred in respect to this fund are offset off the fund amount.

In 2015, Family Bank issued a multicurrency medium term note and listed it on the Nairobi Securities Exchange, Fixed Income Segment on 26 October 2015. The par value accepted by the Bank from investors was Shs 2 billion while the amount received was Shs 1.895 billion. The fixed rate portion was issued at a discount of Shs 122 million .The term of the bond is 5.5 years. The interest rates for the three categories available to the investors were;-

- Fixed rate bond 13.75%
- Mixed rate bond 14%
- Floating rate bond. Referenced 182 day Treasury bill rate subject to a floor of 12.5% and a cap of 17.5%

The effective interest rates for the various loans are as follows:

	2018	2017
	%	%
EIB	9	9
OIKO Credit	10.4	10.4
Corporate Bond	15	15

Due to the difficult macro-economic environment experienced from 2017, the Bank was not in compliance with the agreed limits on the non-performing loan covenant as agreed with both OIKO and EIB. We were however granted conditional waivers by both lenders with revised limits which we remain fully compliant to.
We have in the interim re-classified the maturity of the borrowings to within one year for disclosure purposes in the liquidity analysis in note 4 (b) and (d).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

27 Provisions and Other Liabilities

	Group		Bank	
	2018	2017	2018	2017
	Sh'000	Sh'000	Sh'000	Sh'000
(a) Provisions and accruals				
Provisions and accruals	315,527	270,142	315,527	270,142
Leave pay accrual	34,088	43,196	34,088	42,511
	349,615	313,338	349,615	312,653
(b) Other liabilities				
Cheques for collection	111,294	137,470	111,294	137,470
Advance loan processioning fee	427,017	65,327	427,017	65,119
Accounts payable	100,076	99,120	100,076	99,211
Revenue collected on behalf of revenue authorities	95,921	100,438	95,951	100,438
Other payables	712,370	739,609	690,488	738,412
	1,446,678	1,141,964	1,424,826	1,140,650

Other liabilities are current.

28 Dividends- Group & Bank

Proposed dividends

The directors do not recommend payment of dividends for the year ended 31 December 2018 (2017: Nil).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

29 Deferred income tax

Deferred income tax is calculated using the enacted income tax rate of 30% (2017 - 30%). The movements in the deferred income tax account were as follows:

Group	2018 Sh'000	2017 Sh'000
At start of year	324,880	(24,843)
Impact on adoption of IFRS 9	178,583	-
Profit or loss credit (note 11)	23,840	349,723
At end of year	527,303	324,880

Bank		
At start of year	324,495	(24,883)
Impact on adoption of IFRS 9	178,583	-
Profit or loss credit (note 11)	24,225	349,378
At end of year	527,303	324,495

The deferred tax asset computed at the enacted rate of 30% is attributed to the following items:

	At start of year	Credited / (debited) to profit or loss	Credited to OCI	At end of year
Group				
Deferred income tax assets	**Shs 000**	**Shs 000**	**Shs 000**	**Shs 000**
Provisions	38,250	56,328	178,583	273,161
Excess depreciation over capital allowances	11,694	151,430	-	163,124
Tax losses	287,904	(287,904)	-	-
Revaluation surplus	(12,968)	103,986	-	91,018
Net deferred income tax asset / (liability)	**324,878**	**23,840**	**178,583**	**527,303**
Bank				
Provisions	38,045	56,456	178,583	273,084
Excess depreciation over capital allowances	11,515	152,221	-	163,736
Tax losses	287,904	(287,904)	-	-
Revaluation surplus	(12,969)	103,452	-	90,483
Net deferred income tax asset / (liability)	**324,495**	**24,225**	**178,583**	**527,303**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

30 Share Capital and reserves

a) Share capital

	2018 Sh'000	2017 Sh'000
Authorised:		
1,500,000,000 ordinary shares of Sh 1 each	1,500,000	1,500,000
	========	========
Issued and fully paid ;		
1,287,107,542 ordinary shares of Sh 1 each	1,287,108	1,287,108
	========	========

Movement in issued and fully paid shares

	Number of shares	Share capital Sh '000	Share premium Sh '000	Total Sh'000
At 1 January 2017	1,287,107,542	1,287,108	5,874,662	7,161,770
At 31 December 2017	1,287,107,542	1,287,108	5,874,662	7,161,770
	==========	==========	==========	==========
At 1 January 2018	1,287,107,542	1,287,108	5,874,662	7,161,770
At 31 December 2018	1,287,107,542	1,287,108	5,874,662	7,161,770
	==========	==========	==========	==========

There was no change in the share capital for the year ended 31 December 2018.

b) Nature and purposes of reserves

30.1 Revaluation surplus

This represents solely the revaluation of building and freehold land net of deferred income tax and is non-distributable.

30.2 Statutory reserve

The reserve represents an appropriation from retained earnings to comply with the Prudential guidelines of the Central Bank of Kenya on loan loss provisions. The balance represents excess of impairment provisions determined in accordance with the Prudential guidelines over the impairment provisions recognised in accordance with the International Financial Reporting Standards. The reserve is non- distributable.

30.3 Fair value reserve

The fair value reserve comprise of the cumulative net change in the fair value of available for sale financial assets until the investment is derecognised or impaired. The reserve is non-distributable.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 Notes to the statement of cash flows

a) Reconciliation of profit before taxation to cash flow from operations

	Group		Bank	
	2018	2017	2018	2017
	Sh '000	Sh '000	Sh '000	Sh '000
Profit /(loss) before taxation	434,932	(1,357,638)	419,880	(1,370,841)
Adjustments for:				
Depreciation of property and equipment (note 22)	636,986	758,057	634,705	755,773
Amortisation of intangible assets (note 23)	126,725	143,176	124,896	141,449
Gain on disposal of equipment	-	(9,780)	-	(9,814)
Amortisation of leasehold land (note 24)	4,850	4,621	4,850	4,621
Interest expense on borrowings (note 26)	162,227	319,452	162,227	319,452
Changes in working capital items:				
Cash ratio balance	(628,063)	(58,748)	(628,063)	(58,748)
Loans and advances to customers	(641,239)	6,691,703	(641,239)	6,691,703
Other assets	(378,129)	(1,383,022)	(355,038)	(1,352,303)
Customer Deposit	1,121,059	5,966,898	1,133,583	5,951,788
Provisions and Other liabilities	340,989	390,118	321,138	389,374
Government securities – Amortised cost	746,127	(2,938,266)	746,127	(2,938,266)
Government securities - FVPL	-	251,007	-	251,007
Corporate bonds	449,907	(290)	449,907	(290)
Cash generated from operations	2,376,371	8,777,288	2,372,973	8,774,903

b) Analysis of the balances of cash and cash equivalents as shown in the statement of financial position and notes

	Group		Bank	
	2018	2017	2018	2017
	Sh '000	Sh '000	Sh '000	Sh '000
Cash in hand	3,494,361	3,482,434	3,494,361	3,482,434
Balances with other banking institutions	1,222,738	2,495,298	1,222,738	2,495,298
Balances due to other banking institutions	(247,051)	(201,708)	(247,051)	(201,708)
	4,470,048	5,776,023	4,470,048	5,776,023

For the purpose of the statement of cash flows, 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

32 Operating segments

For management purposes, the Bank is organised into two main operating segments based on products and services as follows:

i) Retail Banking: Includes loans deposits and other transactions and balances with retail customers;
ii) Wholesale Banking: Includes loans deposits and other transactions and balances with corporate and institutional customers.

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss. Income taxes are managed on a group basis and are not allocated to operating segments.
The Group's segment operations are all financial with a majority of revenues deriving from interest. The management relies primarily on net interest revenue to assess the performance of the segment. Interest income is reported net as management primarily relies on net interest revenue as a performance measure, not gross income and expenses. No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Bank's total revenue in 2018 or 2017.

The following table presents income and profit and certain asset and liability information regarding the Group's operating segments,

Profit or loss for the year ended 31 December 2018

	Whole sale banking Sh'000	Retail banking Sh'000	Unallocated Sh'000	Total Sh'000
Interest income	2,822,636	4,233,954	-	7,056,590
Interest expense	(913,581)	(1,370,333)	-	(2,283,914)
Net interest income	1,909,055	2,863,583	-	4,772,676
Other income	973,876	1,460,815	64,281	2,498,972
Operating income	2,882,932	4,324,398	64,281	7,271,648
Depreciation and amortisation	(303,840)	(455,761)	(4,109)	(763,710)
Operating expenses	(1,884,414)	(2,947,771)	(50,962)	(4,883,147)
Impairment charge on loans and advances	(481,709)	(722,564)	-	(1,204,273)
Share of profit subsidiary	-	-	14,414	14,414
Profit before tax	212,968	198,302	23,662	434,932
Tax expense	(74,014)	(111,020)	(5,682)	(190,716)
Profit after tax	138,955	87,282	17,980	244,216

NOTES TO THE FINANCIAL STATEMENTS (Continued)

32 Operating segments (continued)

Profit or loss for the year ended 31 December 2017

	Whole sale banking	Retail banking	unallocated	Total
	Sh'000	Sh'000	Sh'000	Sh'000
Interest income	2,819,156	4,228,734	-	7,047,889
Interest expense	(1,067,153)	(1,600,729)	-	(2,667,882)
Net interest income	1,752,003	2,628,005	-	4,380,008
Other income	840,736	1,261,103	71,363	2,173,202
Operating income	2,592,739	3,889,108	71,363	6,553,210
Depreciation and amortisation	(359,291)	(538,937)	(4,176)	(902,404)
Operating expenses	(2,392,419)	(3,588,629)	(109,773)	(6,090,821)
Impairment charge on loans and advances	(372,572)	(558,858)	-	(931,430)
Share of profit subsidiary	-	-	13,807	13,807
Profit before tax	(531,544)	(797,316)	(28,779)	(1,357,639)
Tax (expense) / Credit	144,506	216,759	(4,415)	356,849
Loss after tax	(387,038)	(580,557)	(33,194)	(1,000,789)

Statement of financial position as at 31 December 2017

	Whole sale banking	Retail banking	unallocated	Total
Assets				
Segment assets	27,595,245	41,392,864	-	68,988,109
Un-allocated assets	-	-	146,827	146,827
Total assets	27,595,245	41,392,864	146,827	69,134,935
Liabilities and equity:				
Segment liabilities	27,678,807	41,518,207	-	69,197,014
Un-allocated liabilities	-	-	(62,079)	(62,079)
Inter-segment lending	(57,857)	(86,785)	144,162	-
Total liabilities and equity	27,620,950	41,431,423	82,563	69,134,935
Other disclosures				
Capital expenditure	130,128	162,660	32,532	325,321

NOTES TO THE FINANCIAL STATEMENTS (Continued)

32 Operating segments (continued)

Statement of financial position as at 31 December 2018

	Whole sale banking Sh' 000	Retail banking Sh' 000	unallocated Sh' 000	Total Sh' 000
Assets				
Segment assets	26,712,067	40,121,273	-	66,833,340
Un-allocated assets	-	-	177,725	177,725
Total assets	26,712,067	40,121,273	177,725	67,011,065
Liabilities and equity:				
Segment liabilities	40,181,493	26,882,136	-	67,063,629
Un-allocated liabilities	-	-	(52,564)	(52,564)
Inter-segment lending	(61,737)	(92,605)	154,342	-
Total liabilities and equity	40,119,756	26,789,531	101,778	67,011,065
Other disclosures				
Capital expenditure	28,855	19,236	-	48,091

33 Operating lease arrangements

At the end of the reporting period, the Group had contracted with tenants for the following future lease payables.

	2018 Sh'000	2017 Sh'000
Year 1	581,487	568,840
Year 2 - 3	1,265,385	1,237,893
Year 4 - 5	1,429,708	1,398,633
Above 5 years	1,735,395	1,731,606
	5,011,975	4,936,972

Operating leases relate to the leased property. The lease terms range between 1 to 10 years, with an option to extend for a further period between 1 to 10 years. All operating lease contracts contain market review clauses in the event that the lessee exercises its option to renew. The lessee does not have an option to purchase the property at the expiry of the lease period. The operating lease contracts are cancellable.

At the end of the reporting period, the Group had contracted with tenants for the following future lease receivables.

	2018 Sh'000	2017 Sh'000
Year 1	9,322	8,755
Year 2 - 3	17,175	9,387
Year 4 - 5	11,356	9,711
Above 5 years	-	10,925
	37,853	38,778

NOTES TO THE FINANCIAL STATEMENTS (Continued)

33 Operating lease arrangements (continued)

Operating leases relate to the freehold property. The lease terms range between 5 to 10 years, with an option to extend the period. All operating lease contracts contain market review clauses in the event that the lessor exercises its option to renew. The lessee does not have an option to purchase the property at the expiry of the lease period. The operating lease contracts are cancellable.

34 Contingencies and commitments including off balance sheet items

a) Contingent liabilities

In common with other financial institutions, the group 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.

	2018 Sh'000	2017 Sh'000
Guarantees	3,970,214	3,259,403
Letters of credit	144,145	130,878
	4,114,359	3,390,281
	=======	=======
Litigations against the Group	187,121	237,018
	=======	=======

Nature of contingent liabilities:

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

Letters of credit commit the group 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 group will only be required to meet these obligations in the event of the customer's default.

Concentrations of contingent liabilities are covered under note 4.

Litigations against the Group

Litigations against the group relate to civil suits lodged against the group 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 liability will accrue from the pending suits.

b) Commitments to extend credit

	2018 Sh'000	2017 Sh'000
Undrawn formal stand-by facilities, credit lines and other commitments to lend	2,018,181	4,230,868
	========	========

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 group may withdraw from its contractual obligation to extend credit by giving reasonable notice to the customer.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

34 Contingencies and commitments including off balance sheet items (Continued)

	2018 Sh'000	2017 Sh'000
c) Capital commitments		
Authorised and contracted for	243,122	663,901
Authorised but not contracted for	-	135,000
	======	======

35 Related party transactions

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 Group by directors, their associates and companies associated to directors. Advances to customers at 31 December 2018 include advances and loans to companies associated with the directors.

	Group		Bank	
	2018	2017 Sh '000 Sh '000	2018 Sh '000	2017 Sh '000
(a) Loans and advances				
At 1 January	3,269,083	3,828,353	3,269,083	3,828,353
Additions	1,057,789	727,666	1,057,789	727,666
Interest charged	278,872	266,376	278,872	266,376
Repayments	(1,015,185)	(1,553,312)	(1,015,185)	(1,553,312)
At 31 December	3,590,559	3,269,083	3,590,559	3,269,083
	=========	=========	=========	=========

As at 31 December 2018 loans and advances to staff amounted to Sh 1,145,484,922 (2017 – Sh 1,400,556,552). The loans and advances to related parties are performing and adequately secured.

	Directors Sh '000	Companies associated to directors Sh '000	Total Sh '000
(b) Deposits – Group and bank			
At 1 January 2017	27,228	340,779	368,007
Withdrawals	(14,190)	458,502	444,312
At 31 December 2017	13,038	799,281	812,319
At 1 January 2018	417,921	806,687	1,224,608
Withdrawals	(13,038)	(799,281)	(812,319)
At 31 December 2018	404,883	7,406	412,289
	========	========	========

NOTES TO THE FINANCIAL STATEMENTS (Continued)

35 Related party transactions (continued)

Key management compensation

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

	2018 Sh'000	2017 Sh'000
Short term benefits		
Salaries and other benefits	99,027	125,445
Directors' emoluments	44,651	93,539
	143,678	218,984

36 Family Bank Foundation

The Bank has control over The Family Group Foundation ("the Foundation") as per the provisions of IFRS 10 Consolidated Financial Statements. Control in this case is achieved through the Bank's contributions to the Foundation which indicate power over the Foundation and its ability to influence the Foundation's activities, as well as the reputational dividend from the Foundation's name.

The Foundation is registered in Kenya and its principal activity is to provide financial support in the education of needy students in Kenya. Its registered office is Daykio Plaza, Ngong Road, Nairobi.

Except for Kshs 42m (2017: Kshs 46m) contributions by the Bank to the Foundation which have been included as expenses in Note 9 of the financial statements, other intercompany transactions and interactions between the Foundation and the Bank were immaterial. These financial statements are not consolidated as a result.

37 Prior year restatement

The prior year financial statements have been restated to recognise interest income on non-performing loans that should have been recognised in line with the requirements of IAS 39. The interest income ought to have been recognised on the amortised balance i.e. net of specific impairments, using the original effective interest rate of the impaired financial assets. The interest recognised was assessed as fully impaired and therefore the adjustment had no impact on the statements of financial position, changes in equity or cash flows.

The effect of the restatement on the statement of comprehensive income, which is effectively a gross up of the interest income and credit impairment charges for the year ended 31 December 2017 is as follows;
Group statement of comprehensive income

	2017 Sh'000	Increase/ (decrease) Sh'000	Restated 2017 Sh'000
Interest income	7,047,889	513,033	7,560,922
Net interest income	4,380,008	513,033	4,893,040
Impairment losses on loans and advances	(931,430)	(513,033)	(1,444,463)
loss before taxation	(1,357,638)	-	(1,357,638)
Income tax credit	356,850	-	356,850
Loss for the year	(1,000,788)	-	(1,000,788)

NOTES TO THE FINANCIAL STATEMENTS (Continued)

37 Prior year adjustments (continued)

Bank statement of comprehensive income

	2017 Sh'000	Increase/ (decrease) Sh'000	Restated 2017 Sh'000
Interest income	7,047,889	513,033	7,560,922
Net interest income	4,373,771	513,033	4,886,804
Impairment losses on loans and advances	(931,430)	(513,033)	(1,444,463)
Loss before taxation	(1,370,841)	-	(1,370,841)
Income tax credit	361,264	-	361,264
Loss for the year	(1,009,577)	-	(1,009,577)

PROXY FORM

Shareholder's Name: ……...
Share Account No. ……...

The Company Secretary
Family Bank Limited
8th Floor, Family Bank Towers.
P.O Box 74145-00200
Nairobi

PROXY FORM

I/We …….....of P.O Box……being a shareholder(s) of Family Bank Limited, appoint ……..... of P.O. Box …… …….. and failing him / her, the chairman of the meeting to be my/our proxy, to vote on my/our behalf at the Annual General Meeting of the Bank to be held on Thursday, 30th May 2019 at 10.00am at Kenyatta International Conference Centre, Amphitheatre and at any adjournment thereof.

This form is to be used in favor or against the resolution and unless otherwise instructed the proxy will vote as he/she deems fit.
As witnessed by my/our hand this ……day of …….. 2019
Signed…….....…… Signed…….…….....…….…….
ID No…….…….....… ID No……..…….....…….

NOTES

1. A member who is unable to attend the meeting is entitled to appoint a proxy to attend and vote on his or her behalf.
2. A proxy need not be a member
3. In the case of a corporate body, the proxy must be under its common seal or under the hand of an officer or attorney duly authorized in writing.
4. Joint account holders must state their joint names and sign according to their signing mandates.
5. The proxy must be delivered to the bank's registered office not less than forty eight hours before the time for holding the meeting or adjourned meeting, failing which it will be invalid.

Shareholder's Admission Form

Please complete this form and note that it must be produced at the Annual General Meeting by you or your proxy for admission.

Name…… ID Number.....

Shareholder's Share Account No……. Signature .....…….....

Family Bank
With you, for life

Family Bank Limited is regulated by the Central Bank of Kenya

Notes

Notes

Notes

BRANCHES

Family Bank
With you, for life

BRANCH NAME	BRANCH CODE
Kiambu	001
Githunguri	002
Sonalux	003
Gatundu	004
Thika	005
Murang'a	006
Kangari	007
Kiria-ini	008
Kangema	009
JKIA	010
Othaya	011
Kenyatta Avenue - Nairobi	012
Cargen	014
Laptrust - Nairobi	015
City Hall - Nairobi	016
Kasarani	017
Nakuru Finance	018
Nakuru Market	019
Kutus	020
Dagoretti	021
Kericho	022
Nyahururu	023
Ruiru	024
Nyamira	026
Kisii	027
Kisumu Express	028
Narok	029
Kangemi	030
Industrial Area - Nairobi	031
Makongeni - Thika	032
Donholm	033
Utawala	034
Family Bank Towers Retail	035
Mlolongo	036
Ol-Kalou	037
KTDA Retail	038
Gateway Mall - Nairobi	039
Kariobangi	041
Gikomba Area 42	042
Gikomba	043
Kahawa West	044
Githurai	045
Kilimani	046
Limuru	047
Westlands	048
Kagwe	049

BRANCH NAME	BRANCH CODE
Banana	051
Ruaka	052
Naivasha	053
Chuka	054
Nyeri	055
Karatina	056
Kerugoya	057
River Road West - Nairobi	058
River Road - Nairobi	059
Kayole	061
Nkubu	062
Meru	063
Nanyuki	064
KTDA Corporate	065
Ongata Rongai	066
Kajiado	067
Family Bank Towers Corporate	068
Ngara	069
Kitengela	071
Kitui	072
Machakos	073
Migori	074
Embu	075
Mwea	076
Bungoma	077
Kakamega	078
Busia	079
Mumias	081
Eldoret West	082
Molo	083
Bomet	084
Eldoret	085
Maua	086
Litein	087
Wote	088
Ukunda	091
Mombasa Digo Road	092
Kitale	093
Mtwapa	094
Mombasa Nkrumah Road	095
Mombasa Kenyatta Avenue	096
Kapsabet	097
Malindi	098
Kikuyu	102

Family Bank Towers, Muindi Mbingu Street | P.O. Box 74145 - 00200, Nairobi, Kenya | Tel: 254-2-3252 445/0703095 445
Email: info@familybank.co.ke | Website: www.familybank.co.ke