PARAMOUNT BANK

Enabling you to reach your peak

2016

ANNUAL REPORT AND FINANCIAL STATEMENTS

Contents

BRANCH NETWORK

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Bank to Bank Transfer

PesaLink

Easy . Affordable . Instant .

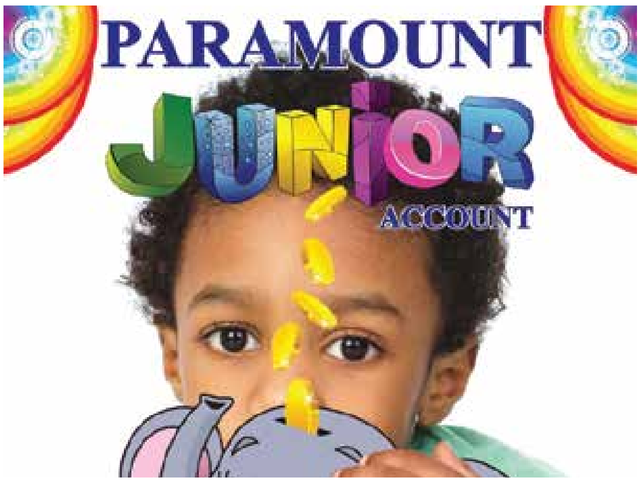
Bureau De Change

Vision - To be one of the best regarded Banks in Kenya providing the highest quality products and services.

Parabank Insurance Agency

Mission - To develop a motivated professional staff that will profitably deliver high quality customer services that fill the financial needs of our customers and their businesses.

Credit Card with Chip + Pin



CORPORATE INFORMATION

DIRECTORS

Anwarali Padany - Chairman
Ayaz Merali - Chief Executive Officer (CEO)
Noorez Padamshi
Muhammed Mujtaba
Mercy Kamau
Angela Musimba (Resigned 25th April 2016)
Eunice Wamaitha (Appointed 1st December 2016)

AUDIT COMMITTEE

Angela Musimba - (Resigned 25 April 2016) Chairlady
Eunice Wamaitha (Appointed 1st December 2016)
Noorez Padamshi
Mercy Kamau
Kapil Deo Sharma
Henry Onkunya

CREDIT COMMITTEE

Mercy Kamau - Chairlady
Angela Musimba (Resigned 25th April 2016)
Eunice Wamaitha (Appointed 1st December 2016)
Anwarali Padany
Ayaz Merali
Muhammed Mujtaba
Michael Riitho

ASSET LIABILITY COMMITTEE

Ayaz Merali - Chairman
Nicholas Odera
Muhammed Mujtaba
Fred Maina

RISK MANAGEMENT COMMITTEE

Angela Musimba (Resigned 25th April 2016) - Chairlady
Eunice Wamaitha (Appointed 1st December 2016)
Anwarali Padany
Noorez Padamshi
Stanley Ngaruiya Ndungu

BOARD NOMINATIONS AND REMUNERATION COMMITTEE

Anwarali Merali - Chairman
Noorez Padamshi
Angela Musimba (Resigned 25th April 2016)
Eunice Wamaitha (Appointed 1st December 2016)

COMPANY SECRETARY

Winniefred Nyagoha Jumba
Certified Public Secretary (Kenya)
C/o Livingstone Associates
P O Box 30029 Nairobi - GPO 00100

REGISTERED OFFICE

LR Plot No 1870/IX/140
4th Floor, Sound Plaza
Woodvale Groove
P O Box 14001Nairobi - Westlands 00800

AUDITORS

Deloitte & Touche
Certified Public Accountants (Kenya)
Deloitte Place, Waiyaki Way, Muthangari
P O Box 40092 Nairobi GPO 00100

PRINCIPAL CORRESPONDENTS

Deutsche Bank AG, Germán
Deutsche Bank Trust Co, New York
Habib Bank Limited, London
Standard Bank of South Africa, Johannesburg
HDFC Bank, India
BMCE, Spain

LEGAL ADVISERS

Walker Kontos - Hakika House, Bishops Road
P O Box 60680 - Nairobi City Square 00200

Ngatia & Associates Advocates - Bishop Garden Towers, 1st Ngong Avenue
P O Box 56688 - Nairobi City Square 00200

Mwaniki Gachoka & Co Advocates
Design Centre, 3rd Floor Office suite no.1A & 3A
P O Box 13439 Nairobi GPO 00800

REPORT OF THE DIRECTORS

The directors present their report together with the audited financial statements of Paramount Bank Limited (the "bank") and its subsidiaries (together, the "Group") for the year ended 31 December 2016, which disclose its state of affairs. In accordance with Section 42 of the sixth schedule transitional and savings provisions of the Companies Act, 2015, this report has been prepared in accordance with section 157 of the repealed Companies Act, as if this repeal had not taken effect.

INCORPORATION

The bank and its subsidiary, Parabank Insurance Agency Limited, are both incorporated in the Republic of Kenya under the Companies Act and are domiciled in Kenya.

ACTIVITIES

The principal activity of the bank, which is licensed under the Banking Act, is the provision of banking, financial and related services. The principal activity of the subsidiary is to provide bank assurance services through insurance agency services.

GROUP RESULTS

The following is the summary of the results for the year ended 31 December 2016:

	Group		Bank	
	2016	2015	2016	2015
	Sh'000	Sh'000	Sh'000	Sh'000
Profit before taxation	104,882	168,204	104,666	168,876
Taxation	1,557	(10,649)	1,622	(10,851)
Profit for the year	106,439	157,555	106,288	158,025

DIVIDENDS

The directors do not recommend the payment of a dividend in respect of the year ended 31 December 2016 (2015: Sh Nil).

DIRECTORS

The present members of the Board of Directors are shown on page 2. The following changes took place in the directorship during the year.

- Mrs. Angela Musimba term as director ended on 25 April 2016
- Mrs. Eunice Wamaitha was appointed on 1st December 2016

AUDITORS

Deloitte & Touche, having expressed their willingness, continue in office in accordance with the provisions of the Kenyan Companies Act, and subject to approval by the Central Bank of Kenya in accordance with Section 24 of the Banking Act.

BY ORDER OF THE BOARD

Secretary

31.03.2017 Nairobi

PARAMOUNT BANK LIMITED
STATEMENT ON CORPORATE GOVERNANCE

The bank's board of directors is responsible for the governance of the bank and is accountable to the shareholders for ensuring that the bank complies with the law, the highest standards of corporate governance and business ethics. The directors attach great importance to the need to conduct the business and operation of the bank with integrity and in accordance with generally accepted corporate practice and endorse the internationally developed principles of good corporate governance.

Board of Directors

The full board meets at least four times a year. The directors are given appropriate and timely information so that they can maintain full and effective control over strategic, financial, operational and compliance issues.

Except for direction and guidance on general policy, the board has delegated authority for conduct of day-to-day business to the Chief Executive Officer. The board nonetheless retains responsibility for establishing and maintaining the Group's overall internal control over financial, operational and compliance issues. Details of attendance for each member of board are as below.

Directors	No. of meetings attended 2016
Anwarali Padany - (Chairman)	4
Ayaz Merali - Chief Executive Officer (CEO)	4
Noorez Padamshi	4
Muhammed Mujtaba	4
Mercy Kamau	3
Angela Musimba (Resigned 25th April 2016)	1
Eunice Wamaitha (Appointed 1st December 2016)	0

Directors' remuneration

Two executive directors are paid a monthly salary and are eligible for pension scheme membership. The other two non-executive directors are paid sitting allowance for Board meetings and Board sub-committee meetings.

Committees of the Board

Audit Committee

The board has constituted an audit committee that meets as required. Its responsibilities include review of financial information, budgets, development plans, compliance with accounting standards in financial reporting, and liaison with the external auditors, remuneration of external auditors and overseeing internal control systems. Internal and external auditors and other executives attend audit committee meetings as required.

Credit Committee

The board has constituted a credit committee that meets as required. Its responsibilities include a review of the overall lending policy of the bank, ensuring that there are effective policies and procedures to effectively manage credit risk, monitor and review all matters, which may materially impact the present and future quality of the institution's credit risk management.

Assets Liability Committee

The board has constituted an Assets and Liabilities Committee (ALCO) that meets as required Its responsibilities include deriving the most appropriate strategy in respect of the assets and liabilities of the bank given future expectations, changes and consequence of liquidity constraints, interest rate movements, changes in prices and foreign exchange exposures.

Risk Management Committee

The board has constituted a Risk Management Committee that meets as required. Its responsibilities include carrying out risk assessment and putting in place risk indicators and monitoring the risk.

Board Nominations and Remuneration Committee

The board has constituted Nominations and Remuneration Committee.The committee deals with all aspects of appointment of an institution's directors, review the mix of skills and experience and other qualities in order to assess the effectiveness of the board. The committee is also responsible for overseeing the compensation system in place on behalf of the Board of Directors.

Statement on risk management

The Bank recognises the responsibility to manage risks related to its business as a financial institution. The bank has built strong internal systems to ensure that sound banking practices results in income streams that are commensurate with the risks taken.

The Integrated Risk Management Policy of the bank is fully committed to adopting best practices in identifying, measuring, controlling and monitoring the risks faced.

Corporate Governance Statement on Conflict of Interest

The board of directors has approved a code of conduct that gives disclosure guidance on potential conflicts of interest situations. Reporting procedures are in place for this. The code of conduct has to be signed annually by all staff members.

The bank aims at:

- Integrating risk management into the culture of the organization.
- Eliminating or reducing risk to the lowest acceptable levels.
- Developing risk sensitivity as a core competency of all stakeholders.
- Continually identifying potential risks and pro-actively mitigating them.
- Focusing on key risks and controlling them cost-effectively.

The bank has developed a risk infrastructure that is appropriate to the size and volatility of the business. Decision making at all levels are inspired by the aspiration to be a risk intelligent organization. Risk management is used as an enabler to exploit the potential for increased business by taking informed risks with awareness and control.

Compliance

The Bank operates within the requirements of the Banking Act, among other Acts, and adopts certain universally accepted principles in the areas of human rights, labour standards and environment in its commitment to best practice. Additionally, the Group prepares its financial statements in accordance with International Financial Reporting Standards (IFRS).

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Director **Director**

31st March 2017

CHAIRMAN'S REPORT FOR YEAR 2016

On behalf of the Board of Directors of Paramount Bank, I would like to present to you the Audited Financial results for the year 2016.

These are challenging times for the banking industry in terms of the dynamic operating environment influenced by domestic and international factors. The industry has been in recovery mode since the turmoil experienced in 2015 due to collapse of a medium sized bank. Thus the closure of another bank medium sized bank in April 2016 made the operating environment fragile. In addition to the above factors, the industry and the bank as well had to contend with the Amendment to the Banking Act 2016 which introduced interest rate capping on loans to not more than 4% above the Central Bank Rate (CBR) and deposit rates not to be below 70% of the same CBR. The capping of interest rates has led to changes in the bank's business model with emphasis on quality lending to mitigate credit risks. This will take time to be fully realized as adjustments are made to fine tune the bank's operations in the new environment. This is the new normal and reality of banking business in this country. The bank's Board and Management are conscious of the above fact and will continue to deploy all available resources in enhancing stakeholder value.

Despite being a challenging year, the bank still posted reasonable figures compared to 2015. Profit before tax declined to 105 million from 168 million the previous year. This was on the back of reduced lending activities in the last half of the year leading to a drop in operating income by about 5% to 481 million. However, operating expenses also went down by about 37% to 316 million instead of 333 million in 2015. Earnings per share thus dropped to 108.08 shillings compared to 157.55 in 2015 but total shareholders' funds increased to 1.644 billion shillings from 1.536 billion, reflecting the long term view of shareholders in having a strong balance sheet anchored on a sound capital base.

The bank's liquidity and capital base remains solid in supporting its business plans. Indeed, the new Kisumu branch was officially opened this year by Dr. Said Ali Matano – Executive Director of Lake Victoria Basin Commission. This was statement of intent on the part of the bank to increase its footprints in the counties since they are the vehicles through which national development will be achieved. The bank also continues to invest in technology so as to provide convenient and reliable services to clients. The bank is now online with the PESALINK service that enables customers to transfer funds of upto 1 million shillings to other bank accounts using their mobile phones.

These are challenging times but they also offer tremendous opportunities to both the bank and its clients. The Board intends to realize this vision through sustained investments and growth that will yield value to all stakeholders.

CHAIRMAN'S REPORT FOR YEAR 2016 (Continued)

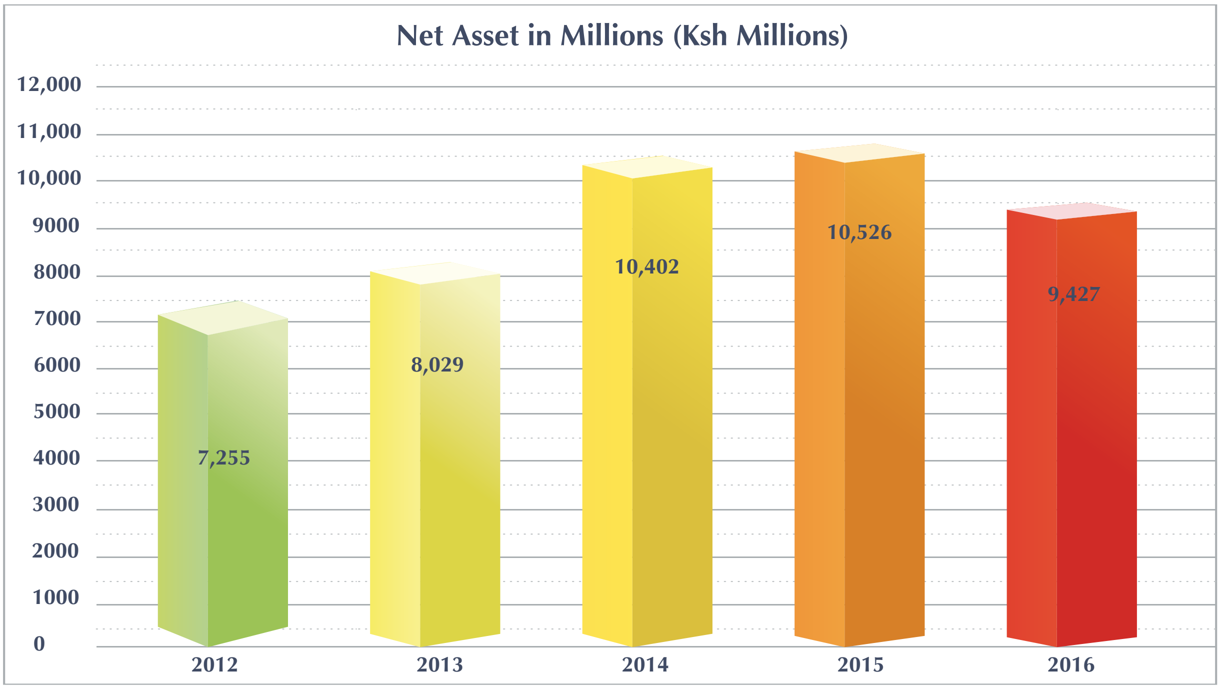
Finally, on behalf of the Board, I would like to wish all our stakeholders a peaceful elections year and prosperity in all their undertakings.

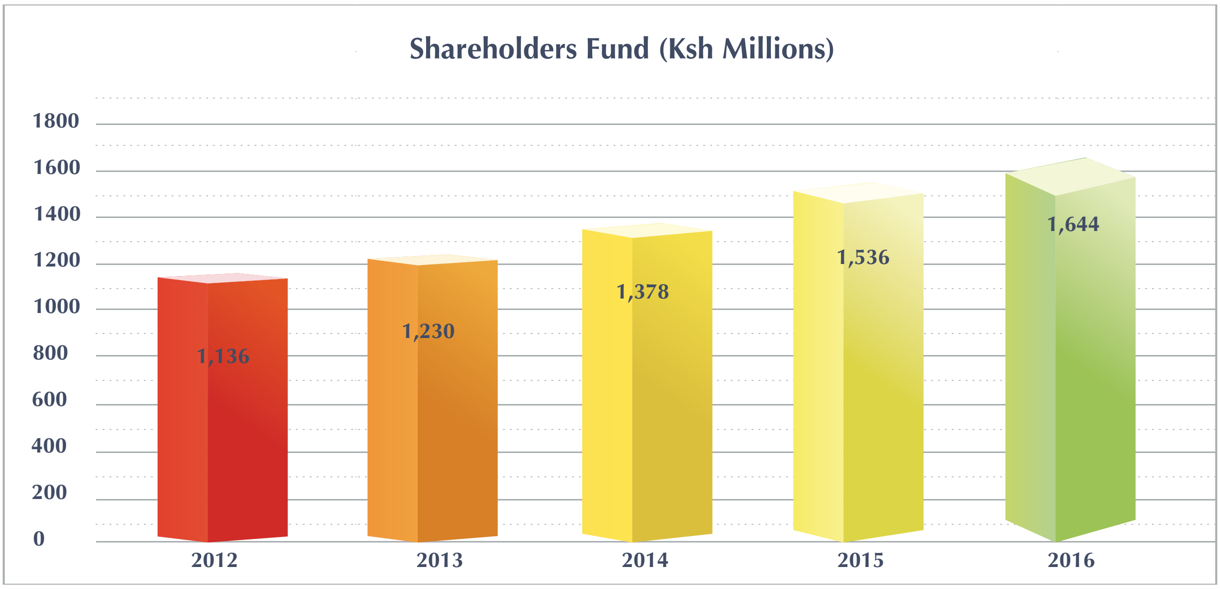
Thank you.

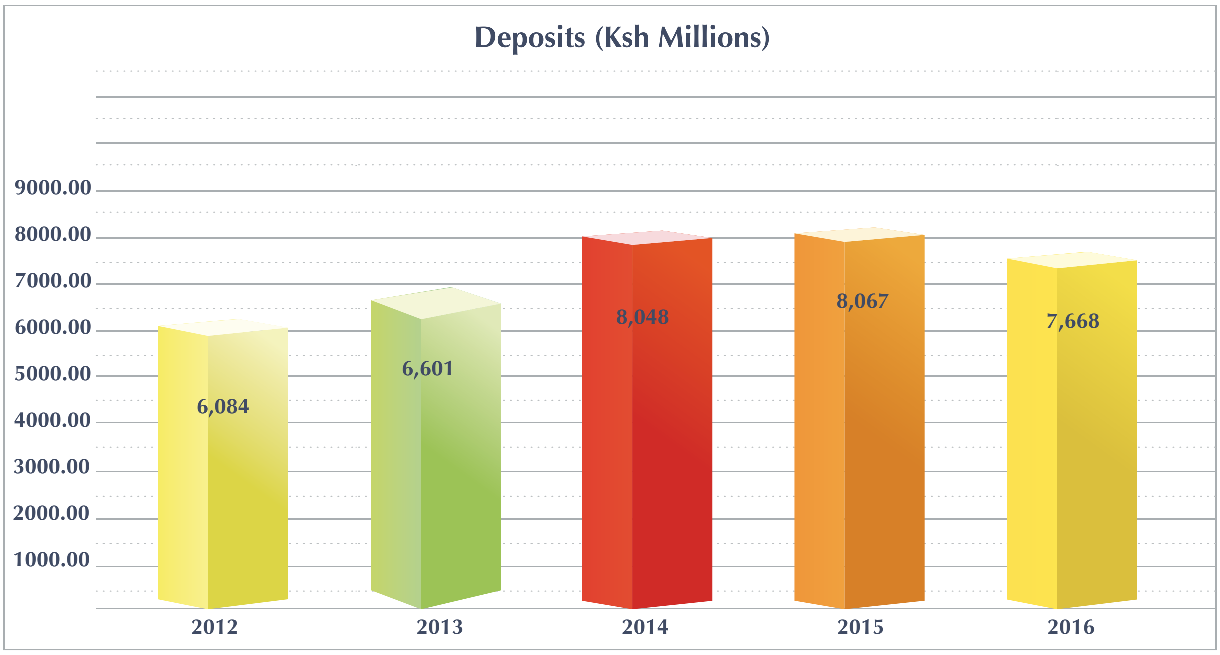
Anwarali Padany.

Chairman.

GRAPHIC REPORT

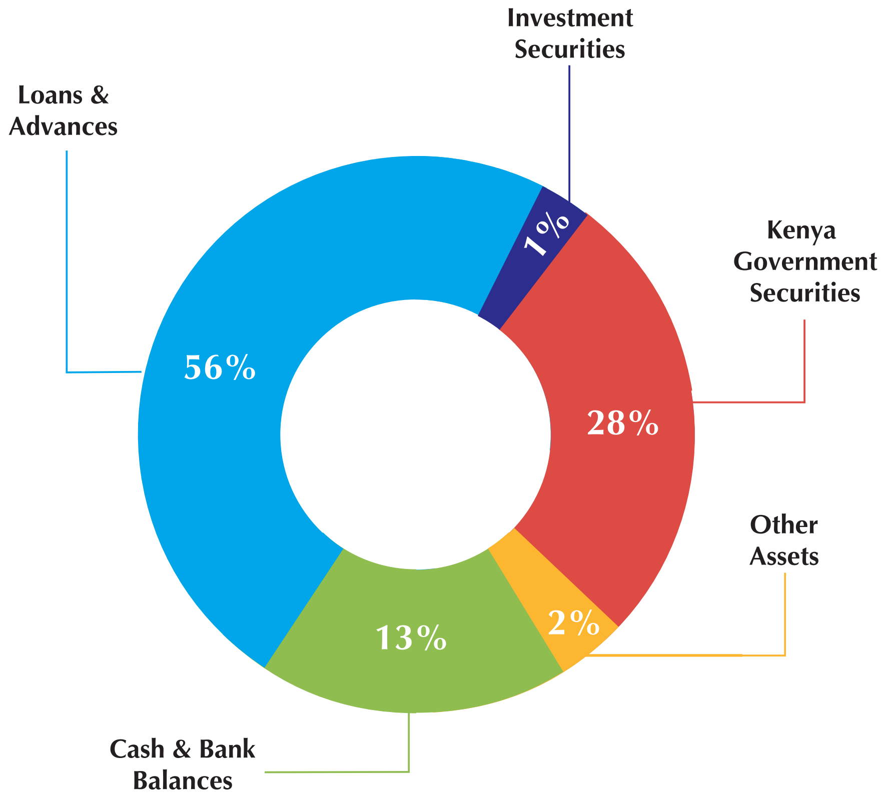




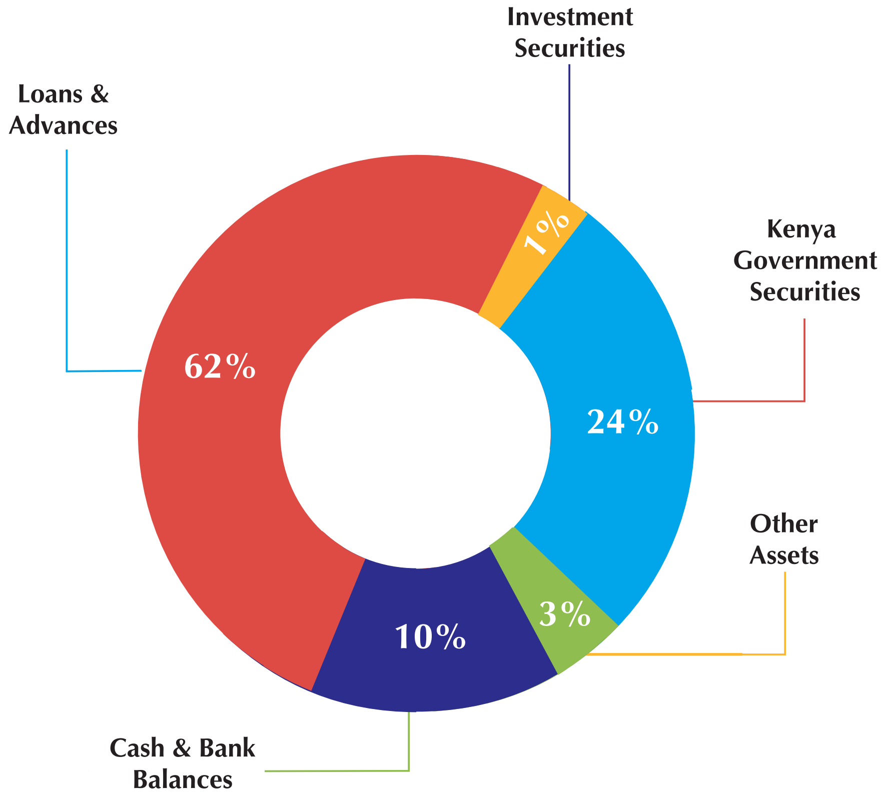


GRAPHIC REPORT

% Assets Distribution 2015



% Assets Distribution 2016



KISUMU BRANCH Official Opening On 24th April 2017

Chief guest DR. Said Ali Matano
Chairman - Mr. Anwarali Padany(Right)
CEO - Mr. Ayaz Merali (Left)

Cutting of the ribbon by chief guest DR. Said Ali Matano.

CEO Mr. Ayaz Merali giving keynote speech to customers and guests.

Guests and Clients sampling refreshments.

CEO Mr. Ayaz Merali with Kisumu branch staff and other senior staff members.

Left to Right:
1. George Ochieng - Client
2. Fred Maina - GM Operations
3. Nicholas Odera - Chief Manager Treasury

Award winning 2017 for the
BANK WITH THE LOWEST CHARGES

Think Business 1st Runner up trophy for bank with lowest charges SME's.

Chairman - Mr. Anwarali Padany (Centre)
CEO - Mr. Ayaz Merali (Right)
Executive Director - Muhammed Mujtaba (Left)

Chairman, Executive Director & CEO of the bank with Unit Heads of Departments (Men).

CFO - Mr. Kapil Sharma and Legal Consultant - Timothy Kimani.

Chairman & CEO of the bank together with Senior Heads of Departments (Ladies).

Bank Directors with head office Staff Members celebrating the Award.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Kenyan Companies Act, 2015 requires the directors to prepare financial statements for each financial year that give a true and fair view of the financial position of the bank and its subsidiary as at the end of the financial year and of its profit or loss for that year. It also requires the directors to ensure that the bank and its subsidiary maintains proper accounting records that are sufficient to show and explain the transactions of the Group and disclose, with reasonable accuracy, the financial position of the Group. The directors are also responsible for safeguarding the assets of the bank and its subsidiary, and for taking reasonable steps for the prevention and detection of fraud and error.

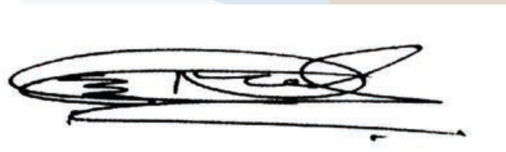
The directors accept responsibility for the preparation and presentation of these financial statements in accordance with the International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. They also accept responsibility for:

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

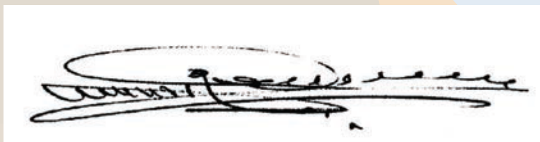
Having made an assessment of the bank and its subsidiary's ability to continue as a going concern, the directors are not aware of any material uncertainties related to events or conditions that may cast doubt upon the bank and its subsidiary's ability to continue as a going concern.

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

Approved by the board of directors on 31st March 2017 and signed on its behalf by



Director



Director

Deloitte & Touche Certified Public Accountants (Kenya)
Deloitte Place, Waiyaki way, Muthangari
P.O.Box 40092 - GPO 00100 Nairobi, Kenya

Tel: +254 (20) 423 0000 I +254 (0) 719 039 000

Dropping Zone No. 92
Email: admin@deloitte.co.ke
www.deloitte.com

Deloitte.

INDEPENDENT AUDITORS' REPORT
TO THE MEMBERS OF PARAMOUNT BANK LIMITED

Opinion

We have audited the accompanying consolidated financial statements of Paramount Bank Limited set out on pages 18 to 68, which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statement of profit or loss and other comprehensive income, the statement of changes in equity and the consolidated statement of cash flows for the year then ended, and the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group and Bank as at 31 December 2016 and of its consolidated 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 and the Banking Act.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISA"). 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. We have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion

Other information

The directors are responsible for the other information, which comprises the information included in the report of directors and the statement of corporate governance and the chairman's report. The other information does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained 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.

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, the requirements of the Kenyan Companies Act, the Banking Act and for such internal controls as directors determine are 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. Those charged with governance are responsible for overseeing the Group's financial reporting process.

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 ISA's 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.

- 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. Refer to the going concern uncertainty included under key audit matters.

- 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 entity or business activities within the Group to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain responsible for our audit opinion

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

We also provide those charged with governance 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 those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters.

Report on Other Legal and Regulatory Requirements

As required by the Kenyan Companies Act 2015, we report to you, based on our audit, that:

i) we have obtained all the information and explanations, which to the best of our knowledge and belief, were necessary for the purposes of our audit;

ii) in our opinion, proper books of account have been kept by the group, so far as appears from our examination of those books; and

iii) the group's statement of financial position (balance sheet) and statement of profit or loss (profit and loss account) are in agreement with the books of account.

The engagement partner responsible for the audit resulting in this independent auditors' report is **CPA FRED OKWIRI - P/NO. 1699.**

Deloitte & Touche

Certified Public Accountants (Kenya)
31 March 2017

CONSOLIDATED AND BANK STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2016

		Group		Bank	
		2016	2015	2016	2015
	Note	Sh'000	Sh'000	Sh'000	Sh'000
INTEREST INCOME	4	1,182,008	1,340,983	1,182,008	1,340,983
INTEREST EXPENSE	5	(886,321)	(784,770)	(886,321)	(784,770)
NET INTEREST INCOME		295,687	556,213	295,687	556,213
Fees and commission income	6	58,737	73,344	55,787	71,584
Gains on foreign exchange dealings	7	12,222	13,152	12,222	13,152
Other operating income	8	11,637	6,569	11,637	6,569
Fair value gain/(loss) on treasury bonds	15(c)	102,988	(135,246)	102,988	(135,246)
OPERATING INCOME		481,271	514,032	478,321	512,272
Operating expenses	9	(316,056)	(333,483)	(313,322)	(331,051)
Impairment losses on loans and advances	18	(60,333)	(12,345)	(60,333)	(12,345)
PROFIT BEFORE TAXATION		104,882	168,204	104,666	168,876
TAXATION CHARGE	11(a)	1,557	(10,649)	1,622	(10,851)
PROFIT FOR THE YEAR		106,439	157,555	106,288	158,025
OTHER COMPREHENSIVE INCOME					
Fair value loss on available for sale treasury bonds		(108)	-	(108)	-
Fair value gain on available for sale infrastructure bonds		1,744	-	1,744	-
		1,636	-	1,636	-
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	15(d)	108,075	157,555	107,924	158,025
		Sh	Sh	Sh	Sh
EARNINGS PER SHARE – Basic and diluted		108.08	157.55	107.92	158.03

CONSOLIDATED AND BANK STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2016

		Group		Bank	
		2016	2015	2016	2015
	Note	Sh'000	Sh'000	Sh'000	Sh'000
ASSETS					
Cash and balances with Central Bank of Kenya	13	758,326	977,494	758,326	977,494
Deposits and balances due from banking institutions	14	215,173	436,239	215,173	436,239
Government securities	15	2,304,319	2,896,653	2,304,319	2,896,653
Corporate bonds	16	114,445	155,701	114,445	155,701
Advances to customers (net)	17	5,799,544	5,871,717	5,799,544	5,871,717
Other assets	19	126,325	100,350	124,676	98,007
Corporate tax recoverable	11(c)	17,453	3,230	17,418	3,195
Equipment	20	71,776	76,373	71,776	76,373
Intangible assets	21	13,963	4,691	13,874	4,572
Deferred taxation asset	22	6,517	4,960	6,380	4,758
Investment in subsidiary	23	-	-	1,000	1,000
TOTAL ASSETS		9,427,841	10,527,408	9,426,931	10,525,709
LIABILITIES					
Customer deposits	24	7,665,713	8,065,202	7,667,902	8,067,107
Deposits and balances due to banking institutions	25	51,334	884,037	51,334	884,037
Other liabilities	26	66,904	42,354	63,486	38,280
TOTAL LIABILITIES		7,783,951	8,991,593	7,782,722	8,989,424
SHAREHOLDERS' FUNDS					
Share capital	27	1,000,000	1,000,000	1,000,000	1,000,000
Retained earnings		559,770	454,118	560,089	454,588
Statutory reserve		82,484	81,697	82,484	81,697
Fair value reserve		1,636	-	1,636	-
TOTAL SHAREHOLDERS' FUNDS		1,643,890	1,535,815	1,644,209	1,536,285
TOTAL SHAREHOLDERS' FUNDS AND LIABILITIES		9,427,841	10,527,408	9,426,931	10,525,709

The financial statements on pages 18 to 68 were approved and authorised for issue by the board of directors on 31st March 2017 and were signed on its behalf by:

_______________________ **Director**

_______________________ **Director**

_______________________ **Chief Executive Officer**

_______________________ **Company Secretary**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2016

	Share capital Sh'000	Retained earnings Sh'000	Statutory reserve Sh'000	Fair value reserve Sh'000	Total Sh'000
At 1 January 2015	1,000,000	316,832	61,428	-	1,378,260
Total comprehensive income for the year	-	157,555	-	-	157,555
Transfer to statutory reserve	-	(20,269)	20,269	-	-
At 31 December 2015	1,000,000	454,118	81,697	-	1,535,815
At 1 January 2016	1,000,000	454,118	81,697	-	1,535,815
Total comprehensive income for the year	-	106,439	-	-	106,439
Other comprehensive income	-	-	-	1,636	1,636
Transfer to statutory reserve	-	(787)	787	-	-
At 31 December 2016	1,000,000	559,770	82,484	1,636	1,643,890

The statutory reserve represents an appropriation from retained earnings in compliance with Central Bank of Kenya's prudential guidelines on impairment of loans and advances. It represents the excess of loans provisions as computed as per the Central Bank of Kenya prudential guidelines over impairment of loans and receivables computed as per IAS 39. The statutory reserve is not distributable.

Retained earnings relates to the cumulative earnings from operations and is distributable.

BANK STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2016

	Share capital Sh'000	Retained earnings Sh'000	Statutory reserve Sh'000	Fair value reserve Sh'000	Total Sh'000
At 1 January 2015	1,000,000	316,832	61,428	-	1,378,260
Total comprehensive income for the year	-	158,025	-	-	158,025
Transfer to statutory reserve	-	(20,269)	20,269	-	-
At 31 December 2015	1,000,000	454,588	81,697	-	1,536,285
At 1 January 2016	1,000,000	454,588	81,697	-	1,536,285
Total comprehensive income for the year	-	106,288	-	-	106,288
Other comprehensive income	-	-	-	1,636	1,636
Transfer to statutory reserve	-	(787)	787	-	-
At 31 December 2016	1,000,000	560,089	82,484	1,636	1,644,209

The statutory reserve represents an appropriation from retained earnings in compliance with Central Bank of Kenya's prudential guidelines on impairment of loans and advances. It represents the excess of loans provisions as computed as per the Central Bank of Kenya prudential guidelines over impairment of loans and receivables computed as per IAS 39. The statutory reserve is not distributable.

Retained earnings relates to the cumulative earnings from operations and is distributable.

CONSOLIDATED BANK STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016

		Group		Bank	
		2016	2015	2016	2015
	Note	Sh'000	Sh'000	Sh'000	Sh'000
CASH FLOWS FROM OPERATING ACTIVITIES					
Cash used in operations	28(a)	(398,639)	(290,459)	(398,639)	(291,643)
Tax paid during the year	11(c)	(14,223)	(35)	(14,223)	-
		(412,862)	(290,494)	(412,862)	(291,643)
CASH FLOWS FROM INVESTING ACTIVITIES					
Purchase of equipment	20	(16,555)	(7,279)	(16,555)	(7,279)
Purchase of intangible assets	21	(10,827)	(494)	(10,827)	(345)
Proceeds from sale of equipment			400		400
Investment in subsidiary	23	-	-	-	1,000
Net cash used in investing activities		(27,382)	(7,373)	(27,382)	(6,224)
INCREASE IN CASH AND CASH EQUIVALENTS		(440,244)	(297,867)	(440,244)	(297,867)
CASH AND CASH EQUIVALENTS AT 1 JANUARY		1,403,503	1,701,370	1,403,503	1,701,370
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	28(b)	963,259	1,403,503	963,259	1,403,503

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2016

1. ACCOUNTING POLICIES

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards.

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

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and interpretations (IFRIC)

i) Relevant new standards and amendments to published standards effective for the year ended 31 December 2016

The following new and revised IFRSs were effective in the current year and had no material impact on the amounts reported in these financial statements.

Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exemption

The amendments clarify that the exemption from preparing consolidated financial statements is available to a parent entity that is a subsidiary of an investment entity, even if the investment entity measures all its subsidiaries at fair value in accordance with IFRS 10. The amendments also clarify that the requirement for an investment entity to consolidate a subsidiary providing services related to the former's investment activities applies only to subsidiaries that are not investment entities themselves

The application of these amendments has had no impact on the Group's consolidated financial statements as the Group is not an investment entity and does not have any holding company company, subsidiary, associate or joint venture that qualifies for designation as an investment entity.

Amendments to IFRS 11 Accounting for Acquisitions of interest in joint operations

The amendments provide guidance on how to account for the acquisition of a joint operation that constitute a business as defined in IFRS 3, Business Combinations. Specifically, the amendments state that the relevant principles on accounting for business combinations in IFRS 3 and other standards should be applied. The same requirements should be applied to the formation of a joint operation if and only if an existing business is contributed to the joint operation by one of the parties that participate in the joint operation. A joint operator is required to disclose relevant information required by IFRS 3 and other standards for business combinations.

The amendment had no impact on the Group's consolidated financial statements as the Group did not have any such transactions in the year.

1. ACCOUNTING POLICIES (Continued)

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and interpretations (IFRIC) (Continued)

i) New standards and amendments to published standards effective for the year ended 31 December 2016 (Continued)

IAS 1 Disclosure Initiative

The amendments clarify that an entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material, and give guidance on the bases of aggregating and disaggregating information for disclosure purposes. However, the amendments reiterate that an entity should consider providing additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, events and conditions on the entity's financial position and financial performance.

In addition, the amendments clarify that an entity's share of the other comprehensive income of associates and joint ventures accounted for using the equity method should be presented separately from those arising from the Group, and should be separated into the share of items that, in accordance with other IFRSs: (i) will not be reclassified subsequently to profit or loss; and (ii) will be reclassified subsequently to profit or loss when specific conditions are met.

As regards the structure of the financial statements, the amendments provide examples of systematic ordering or grouping of the notes.

The application of these amendments has not resulted in any impact on the financial performance or financial position of the Group.

IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation

The amendments to IAS 16 prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment.

The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for amortisation of an intangible asset. This presumption can only be rebutted in the following two limited circumstances:

a) when the intangible asset is expressed as a measure of revenue; or
b) when it can be demonstrated that revenue and consumption of the economic benefits of the intangible asset are highly correlated.

As the Group already uses the straight-line method for depreciation and amortisation of its property and equipment, and intangible assets respectively, the application of these amendments has had no impact on the Group's consolidated financial statements.

Amendments to IAS 16 & IAS 41- Bearer Plants

The amendments define a bearer plant and require biological assets that meet the definition of a bearer plant to be accounted for as property, plant and equipment in accordance with IAS 16 instead of IAS 41. The produce growing on bearer plants continues to be accounted for in accordance with IAS 41.

The application of these amendments has had no impact on the Group's consolidated financial statements as the Group is not engaged in agricultural activities.

1. ACCOUNTING POLICIES (Continued)

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and interpretations (IFRIC) (Continued)

ii) New standards and amendments to published standards effective for the year ended 31 December 2016 (Continued)

Annual Improvements to IFRSs 2012-2014 Cycle

The Annual Improvements to IFRSs 2012-2014 Cycle include a number of amendments to various IFRSs, which are summarised below:

- IFRS 5 - The amendments introduce specific guidance in IFRS 5 for when an entity reclassifies an asset or disposal group) from held for sale to held for distribution to owners (or vice versa). The amendments clarify that such a change should be considered as a continuation of the original plan of disposal and hence requirements set out in IFRS 5 regarding the change of sale plan do not apply. The amendments also clarifies the guidance for when held-for- distribution accounting is discontinued.
- IFRS 7 - The amendments provide additional guidance to clarify whether a servicing contract is continuing involvement in a transferred asset for the purpose of the disclosures required in relation to transferred assets.
- IAS 19 - The amendments clarify that the rate used to discount post-employment benefit obligations should be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. The assessment of the depth of a market for high quality corporate bonds should be at the currency level (i.e. the same currency as the benefits are to be paid). For currencies for which there is no deep market in such high quality corporate bonds, the market yields at the end of the reporting period on government bonds denominated in that currency should be used instead.

The application of these amendments has had no effect on the Group's consolidated financial statements.

iii) New and amended standards in issue but not yet effective in the year ended 31 December 2016

New and Amendments to standards	Effective for annual periods beginning on or after
IFRS 9 Financial Instruments	1 January 2018
IFRS 15 Revenue from contracts with customers	1 January 2018
Amendments to IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses	1 January 2017
Amendments to IAS 7 Disclosure Initiative	1 January 2017
IFRS 16 Leases	1 January 2019

1. ACCOUNTING POLICIES (Continued)

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) interpretations (IFRIC) (Continued)

iii) Impact of new and amended standards on the financial statements for the year ended 31 December 2016 and future annual periods

IFRS 9 Financial Instruments

IFRS 9, issued in November 2009, introduced new requirements for the classification and measurement of financial assets. IFRS 9 was amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition.

Key requirements of IFRS 9:

- All recognised financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement are required to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognised in profit or loss.

- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.

Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.

The directors of the Group are assessing the impact of the application of IFRS 9 in the future. It is not practical to provide a reasonable estimate of this effect until a detailed review has been comple ted.

IFRS 15 Revenue from Contracts with Customers

In May 2014, IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

1. ACCOUNTING POLICIES (Continued)

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and interpretations (IFRIC) (Continued)

iii) Impact of new and amended standards on the financial statements for the year ended 31 December 2016 and future annual periods

IFRS 15 Revenue from Contracts with Customers (Continued)

Specifically, the Standard introduces a 5-step approach to revenue recognition:

Step 1: Identify the contract(s) with a customer
Step 2: Identify the performance obligations in the contract
Step 3: Determine the transaction price
Step 4: Allocate the transaction price to the performance obligations in the contract
Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

Under IFRS 15, an entity recognises revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until a detailed review has been completed.

IFRS 16 Leases

IFRS 16 specifies how an IFRS reporter will recognise, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17.

The directors of the Group do not anticipate that the application of IFRS 16 in the future will have a significant impact on amounts reported in respect of the Group's financial assets and financial liabilities. However, it is not practical to provide a reasonable estimate of the effect of IFRS 16 until a detailed review has been completed.

Amendments to IAS 7 Disclosure Initiative

The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities including both changes arising from cash flows and non-cash changes. The amendments do not prescribe a specific format to disclose finanicing activities. However, an entity may fulfil the disclosure objective by providing a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities.

The amendments apply prospectively for annual periods beginning on or after 1 January 2017 with early application permitted. The directors of the company do not anticipate that the application of these amendments will have a material impact on the Group's consolidated financial statements.

iv) Early adoption of standards

The Group did not early adopt new or amended standards in 2016.

The principal accounting policies applied in the preparation of the financial statements are set out below. These policies have been applied consistently.

1. ACCOUNTING POLICIES (Continued)

Basis of preparation

The consolidated financial statements have been prepared on the historical cost basis except for certain properties and financial instruments that are measured at revalued amounts or fair values at the end of each reporting period, as explained in the accounting policies below.

Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these consolidated financial statements is determined on such a basis.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which is described as follows:-

- Level 1 inputs are quoted in prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement dated.
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly, and
- Level 3 inputs are unobservable inputs for the asset or liability.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Group and entities controlled by the Bank and its subsidiaries. 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 Group 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 Group 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 Group 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 Group's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Group, other vote holders or other parties;
- rights arising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Group 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES (Continued)

Interest income and expense

Interest income and interest expense for all interest bearing financial instruments are accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the bank's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income. Fair value changes on other financial assets and liabilities carried at fair value through profit or loss, are also presented in net trading income included in the profit or loss.

Once a financial asset or a group of financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest that was used to discount the future cash flows for purposes of measuring the allowance for impairment.

Interest income includes interest on loans and receivables, placements with other banks and investments in government securities, and is recognised in the year in which it is earned.

Fees and commission income

In the normal course of business, the bank earns fees and commission income from a diverse range of services to its customers. Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including account servicing fees, investment management fees, placement fees and syndication fees, are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period. Fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

Net trading income

Net trading income arises from the margins which are achieved through market marking and customer business and from changes in market caused by movements in interest and exchange rates, prices and other market variables. It comprises gains less losses related to trading assets and liabilities, and includes all realised and unrealised fair value changes.

Equipment

Equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is calculated on a straight line basis at annual rates estimated to write off the cost of equipment over their expected useful lives using the following rates:

Computers and office equipment	20%
Motor vehicles	25%
Furniture, fittings and office renovations	12.5%

1. ACCOUNTING POLICIES (Continued)

Intangible assets-computer software costs

Generally, costs associated with developing computer software programmes are recognised as an expense incurred. However, a cost that is clearly associated with an identifiable and unique product which will be controlled by the bank and has a probable benefit exceeding the cost beyond one year, are recognised as an intangible asset.

Expenditure which enhances and extends computer software programmes beyond their original specifications and lives is recognised as a capital improvement and added to the original costs of the software. Computer software development costs recognised as assets are stated at cost less amortisation. Amortisation is calculated on a straight line basis over the estimated useful lives not exceeding a period of 5 years.

Impairment of non-financial assets

At the end of each reporting period, the bank 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 company 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. An impairment loss is recognized immediately in profit or loss.

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.

Taxation

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

(i) Current taxation

The corporate 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 bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1. ACCOUNTING POLICIES (Continued)

Taxation (Continued)

(ii) Deferred tax

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.

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 can be utilised. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill 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.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in associates, except where the bank is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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 (and tax laws) that have been enacted or substantively 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 bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

(iii) 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 or directly in the equity respectively.

Foreign currencies

Transactions in foreign currencies during the year are translated at the rates ruling at the time of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into Kenya Shillings at the rates of exchange ruling at the end of each reporting date. Non-monetary items that are measured in terms of historical costs in a foreign currency are not retranslated. Gains and losses on exchange of monetary items are dealt with in the profit or loss in the period in which it arises.

Provisions

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

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1. ACCOUNTING POLICIES (Continued)

Statutory reserve

IAS 39 requires the bank to recognise an impairment loss when there is objective evidence that loans and receivables are impaired. However, Central Bank of Kenya prudential guidelines require the bank to set aside amounts for impairment losses on loans and advances in addition to those losses that have been recognised under IAS 39. Any such amounts set aside represent appropriations of retained earnings and not expenses in determining profit or loss. These amounts are dealt with in the statutory reserve.

Financial instruments

i) Recognition

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

ii) Classification and measurement

Financial assets

The bank classifies its financial assets into the following categories:

- Financial assets at fair value through profit or loss.
- Loans and receivables.
- Held to maturity financial assets.
- Available for sale financial assets.

Management determines the appropriate classification of its investments at initial recognition.

Financial assets at fair value through profit or loss

Financial assets are classified as fair value through profit or loss (FVTPL) when the financial asset is either held for trading or is designated as at at FVTPL). A financial asset is classified as held for trading if acquired principally for the purpose of selling in the short term; or on initial recognition it is part of a portfolio of identified financial instruments that the bank manages together and has a recent actual pattern of short term profit taking; or it is a derivative that is not designated and effective as a hedging instrument. Financial assets at FVTPL are stated at fair value, with gains or losses arising on re-measurement recognised in profit or loss.

Loans and receivables

Loans and receivables including advances originated by the bank are non-derivative financial assets with fixed or determinable payments with fixed maturities that are not quoted in an active market. Loans and receivables are recognised when cash is advanced to borrowers. These are held to maturity and are measured at amortised cost using the effective interest method, less any impairment.

Held to maturity investments

Financial assets with fixed or determinable payments and fixed maturity where the bank has the positive intent and ability to hold to maturity other than loans and receivables originated by the bank are classified as held to maturity investments and are measured at amortised cost using effective interest rate method less any impairments with revenue recognised on an effective yield basis.

1. ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Available-for-sale financial assets

Financial assets that are not (a) loans and receivable originated by the company, (b) held –to-maturity investments, or (c) financial assets held for trading are measured at their fair values. Gains and losses arising from changes in fair value are recognised in other comprehensive income and accumulated in the investments revaluation reserve with the exception of impairment losses; interest calculated using the effective interest method, and foreign exchange gains and losses on monetary assets, which are recognised in profit or loss. Where the investment is disposed and or if determined to be impaired, the cumulative gain or loss previously accumulated in the investments revaluation reserves is reclassified to profit or loss.

Fair values of quoted investments in active markets are based on quoted bid prices. Equity securities for which fair values cannot be measured reliably are measured at cost less impairment.

Impairment and uncollectability of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each reporting date. The bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or 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

If it is probable that the bank will not be able to collect all amounts due (principal and interest) according to the contractual terms of loans and receivables, or held-to-maturity investments carried at amortised cost, an impairment or bad debt loss has occurred. The amount of the loss is the difference between the asset's carrying amount and the present value of expected future cash flows discounted at the financial instrument's original effective interest rate (recoverable amount). The carrying amount of the asset is reduced to its estimated recoverable amount through use of the provision for bad and doubtful debts account. The amount of the loss incurred is included in profit or loss for the period.

The bank assesses whether objective evidence of impairment exist individually for assets that are individually significant and individually or collectively for assets that are not individually significant. If the bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

(i) Assets carried at amortised cost

If there is objective evidence that an impairment loss on financial assets 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 the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial instruments 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.

1. ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Impairment and uncollectability of financial assets (Continued)

(ii) Loans and receivables

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of loans and receivables is established when there is objective evidence that the bank will not be able to collect all amounts due according to the original terms of the loans. The amount of provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the 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 the profit or loss as 'impairment loss on loans and receivables'. When a loan or advance is uncollectible, it is written off against the related allowance account. Subsequent recoveries of amounts previously written off are credited through profit or loss.

Objective evidence that loans and receivables are impaired can include significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group are considered indicators that the loans or receivable is impaired.

In assessing impairment losses, the bank considers the following factors, in each category:

a) Individually assessed loans

- The aggregate exposure to the bank.
- The viability of the customer's business model and its capacity to trade successfully out of financial difficulties and generate sufficient cash flows to meet its debt obligations.
- The realisable value of the security (or other mitigants) and likelihood of successful repossession net of any costs involved in recovery of amounts.
- The amount and timing of expected receipts and, in cases of liquidation or bankruptcy, dividend available.
- The extent and complexity of other creditors commitment ranking pari passu with the bank and the likelihood of other creditors continuing to support the customer.

b) Collectively assessed

- For loans not subject to individual assessment, to cover losses which have been incurred but have not yet been identified.
- For homogeneous groups of loans that are not considered individually significant, where there is objective evidence of impairment.

Homogeneous groups of loans

For homogeneous groups of loans that are not considered individually significant, or in other cases, when the portfolio size is small or when information is insufficient or not reliable enough, the bank adopts a formulaic approach which allocates progressively higher percentage loss rates in line with the period of time for which a customer's loan is overdue. Loss rates are calculated from the discounted expected future cash flows from a portfolio. These rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

1. ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

(ii) Loans and receivables (Continued)   b) Collectively assessed (Continued)

Loan write – offs

An uncollectible loan is written off against the relevant provision for impairment, either partially or in full, when there is no realistic prospect of recovery and the proceeds from realising the security have been substantially or fully recovered.

(iii) Available-for-sale financial assets

In the case of investment classified as available for sale, significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the asset is impaired. Impairment losses on available-for-sale investment securities are recognised by transferring the difference between the amortised acquisition cost and current fair value out of equity to profit or loss. When a subsequent event causes the amount of impairment loss on an available-for-sale debt security to decrease, the impairment loss is reversed through profit or loss.

However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised directly in equity. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

Financial liabilities

After initial recognition, the bank measures all financial liabilities including customer deposits other than liabilities held for trading at amortised cost. Liabilities held for trading (financial liabilities acquired principally for the purpose of generating a profit from short-term fluctuations in price or dealer's margin) are subsequently measured at their fair values.

Derecognition of financial liabilities

Financial liabilities are derecognised when and only when the bank obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

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 on a net basis, or realise the asset and settle the liability simultaneously.

Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with Central Bank of Kenya (CBK), items in the course of collection from other banks, deposits held at call with banks and treasury bills with original maturities of less than three months. Such assets are generally subject to insignificant risk of changes in their fair value, and are used by the bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

Leases

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. Rentals payable under operating leases are charged to profit or loss for the year on a straight-line basis over the term of the relevant lease.

Contingent liabilities

Letters of credit, acceptances, guarantees and performance bonds are generally written by the bank to support performance by a customer to third parties. The bank will only be required to meet these obligations in the event of the customer's default. These obligations are accounted for as off financial position transactions and disclosed as contingent liabilities.

1. ACCOUNTING POLICIES (Continued)

Fiduciary activities

Assets and income arising thereon together with related undertakings to return such assets to customers are excluded from these financial statements where the bank acts in a fiduciary capacity such as nominee, trustee or agent.

Employee benefit costs

i) Bank's defined contribution retirement benefit scheme

The bank operates a defined contribution retirement benefit scheme for its permanent employees. The assets of the scheme are held and administered independently of the bank's assets by an insurance company. The scheme is funded by contributions from both the bank and employees.

ii) Statutory defined benefit obligation pension scheme

The bank contributes to the National Social Security Fund (NSSF). This is a defined contribution scheme registered under the National Social Security Act. Contributions are determined by local statute. The bank's contributions to the statutory retirement benefit scheme are charged to the profit or loss for the year to which they relate.

iii) Other employee entitlements

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the liability for annual leave outstanding at the financial position date.

Comparatives

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

2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING THE BANK'S ACCOUNTING POLICIES

In the process of applying the bank's accounting policies, management has made estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. These are dealt with below:

i) Critical judgements in applying the bank's policies

Impairment losses on loans and receivables

The bank reviews its loan portfolios to assess impairment regularly. In determining whether an impairment loss should be recorded in the profit or loss for the year, the bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans, before a decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a bank, or national or local economic conditions that correlate with defaults on assets in the bank.

Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING THE BANK'S ACCOUNTING POLICIES (CONTINUED)

Financial instruments (Continued)

i) Critical judgements in applying the bank's policies (Continued)

Held -to-maturity investments

The bank follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement. In making this judgement, the bank evaluates its intention and ability to hold such investments to maturity. If the bank fails to keep these investments to maturity other than for the specific circumstances – for example, selling an insignificant amount close to maturity – it will be required to reclassify the entire class as available-for-sale. The investments would therefore be measured at fair value not amortised cost.

ii) Key sources of estimation uncertainty

Equipment

Critical estimates are made by directors in determining the useful lives and residual values for equipment and intangible assets based on the intended use of the assets and the economic lives of those assets. Subsequent changes in circumstances such as technological advances or prospective utilisation of the assets concerned could result in the actual useful lives or residual values differing from initial estimates.

Deferred tax assets

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgement is required to determine the amount of deferred tax asset that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

3. FINANCIAL RISK MANAGEMENT

The Board of Directors retains the overall responsibility for the risk management of the bank. The Board Risk Management Committee (RMC) is responsible for monitoring compliance with the bank's risk management policies and procedures, and review of the adequacy of risk management framework in relation to the risks faced by the bank. The Board Risk Management Committee is assisted in these functions by various management committees which undertake both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Board.

The following are the key risk categories that have been elaborated in these financial disclosures:

- Credit risk
- Liquidity risk
- Market risk : - Interest rate risk / Foreign exchange risk / Price risk
- Capital management
- Operational risk

a) Credit risk

Credit risk refers to the current or prospective risk to earnings and capital arising from an obligator's failure to meet the terms of any contract with the bank or if an obligator otherwise fails to perform as agreed. It arises principally from lending, leasing, trade finance and treasury activities. The bank's credit risk is primarily attributable to its loans and receivables. The amounts presented in the statement of financial position are net of allowances for doubtful advances, estimated by the bank's management based on prior experience and their assessment of the current economic environment.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

a) Credit risk (Continued)

Management of credit risk

The Board of directors has delegated responsibility for the management of credit risk to its Credit Committee (CC).

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

Credit risk is the risk of financial loss to the bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the bank's loans and receivables to customers and other banks and investment securities.

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. Exposure to credit risk is also managed in part by obtaining collateral and corporate guarantees.

Maximum exposure to credit risk before collateral held

The amount that best represents the bank's maximum exposure to credit at the end of the period is analysed as follows:-

	2016 Sh '000	%	2015 Sh '000	%
On balance sheet items				
Items in the course of collection from other banks (note 19)	15,052	-	8,874	-
Deposits and balances due from banking institution (note 14)	215,173	3	436,239	5
Loans and receivables to customers (note 17)	5,799,544	69	5,871,717	63
Government securities (note 15)	2,304,319	27	2,896,653	31
Corporate bonds (note 16)	114,445	1	155,701	1
Total	8,448,533	100	9,369,184	100
Off – balance sheet items (note 29 (a))				
Letters of credit	92,782	25	183,572	39
Letters of guarantee and performance bonds	165,064	44	211,164	45
Bills for collection	117,430	31	75,865	16
	375,276	100	470,601	100
Grand total	8,830,768		9,839,785	

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

a) Credit risk (Continued)

The table below represents the worst case scenario of credit exposure for both years, without taking account of any collateral held or other credit enhancements attached.

Classification of loans and receivables to customers

	Gross loan amount Sh '000	Impairment allowance Sh '000	Net loan amount Sh '000	%
At 31 December 2016				
Neither past due nor impaired	4,090,293	-	4,090,293	70
Past due but not impaired	1,505,566	-	1,505,566	26
Impaired	348,676	(144,991)	203,685	4
Total	5,944,535	(144,991)	5,799,544	100
At 31 December 2015				
Neither past due nor impaired	4,420,952	-	4,420,952	75
Past due but not impaired	1,249,566	-	1,249,566	21
Impaired	304,891	(103,692)	201,199	3
Total	5,975,409	(103,692)	5,871,717	100

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

Neither past due nor impaired

These are well documented facilities granted to financially sound customers where no weaknesses exist. All such facilities are performing in accordance with the contractual terms and are expected to continue doing so. Loans in this category are normally fully protected by the current sound net worth and paying capacity of the borrower. These exposures are categorised as normal in line with Central Bank of Kenya (CBK) prudential guidelines and a provision of 1 % is made and appropriated under statutory reserves.

Past due but not impaired

These are accounts which may be currently protected but, though not past due, reveal weaknesses in the financial conditions or credit worthiness of the borrower. Such weaknesses, if not corrected, may weaken the asset or inadequately protect the bank's position at some future date. These exposures are graded category 2 in line with CBK guidelines.

Impaired

Impaired loans and securities are loans and securities for which the bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan / securities agreement(s). These loans are graded categories 3 to 5 in the bank's internal credit risk grading system. These accounts under CBK guidelines are termed as non-performing loans.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

a) Credit risk (Continued)

Allowances for impairment

The bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loan loss allowance established for banks of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

Collateral held

The bank holds collateral against loans and advances to customers in the form of mortgage interests over property, 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.

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

	2016 Sh '000	2015 Sh '000
Loans and advances to customers		
Discounted value of securities for past due and impaired loans		
90 - 180 days	270,802	71,900
180 days +	148,525	166,711
Total	419,327	238,611

Concentration of risk

The bank has no significant concentration of credit risk, with exposure spread over a diversity of personal and commercial customers as set out in the table below:

i) Advances to customers

	2016 Sh '000	%	2015 Sh '000	%
Real estate	1,562,628	26	1,489,084	25
Social community and personal services	329,036	6	312,250	5
Manufacturing	431,270	7	258,537	4
Transport and communications	251,692	4	260,712	4
Other	3,369,909	57	3,654,826	62
Total	5,944,535	100	5,975,409	100

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

a) Credit risk (Continued)

Concentration of risk (Continued)

ii) Customer deposits

	2016 Sh '000	%	2015 Sh '000	%
Co-operatives societies	-	-	-	-
Private enterprises	5,825,417	76	6,130,999	76
Non profit institutions and individuals	1,840,296	24	1,934,203	24
Total	7,665,713	100	8,065,202	100

iii) Off – balance sheet items

	2016 Sh '000	%	2015 Sh '000	%
Business services	26,269	7	32,942	7
Wholesale and retail	303,974	81	381,187	81
Transport and communications	15,011	4	18,824	4
Other	30,022	8	37,648	8
Total	375,276	100	470,601	100

Summary of credit risk exposure taking into account collateral

	2016 Sh '000	2015 Sh '000
Loans and advances		
Individually impaired		
Grade 5 : Impaired (loss)	-	-
Grade 3 & 4 : Impaired (doubtful)	479,961	304,891
Gross amount	479,961	304,891
Allowance for impairment	(144,991)	(103,692)
Carrying amount	334,970	201,199
Collectively impaired		
Grade 1 : Normal	4,072,662	4,420,952
Grade 2 : Watch	1,391,912	1,249,566
Gross amount	5,464,574	5,670,518
Carrying amount	5,799,544	5,871,717

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

a) Credit risk (Continued)

Write-off policy

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

b) Liquidity risk

Liquidity risk is the risk that the bank cannot obtain the necessary funds to meet its obligations associated with financial instruments as they fall due. The amount of liquidity required depends very much on the banks ability to forecast demand and its access to outside sources. The board of directors has assigned the authority for the management oversight of the liquidity risk policy to the Assets and Liability Committee (ALCO). The committee which is composed of the CEO, Treasury Manager, and other bank officers as necessary review various liquidity and funding decisions and related risks. Formal minutes pertaining to committee actions are recorded and maintained for review by the board of directors.

Liquidity management

The bank manages the liquidity structure of assets, liabilities and commitments so that cash flows are appropriately matched to ensure that all funding obligations are met when due. Banking operations are such that mismatch of assets and liabilities according to their maturity profiles cannot be avoided. However, management ensures that the mismatch is controlled in line with allowable risk levels. Liquidity is managed on a daily basis and incorporates assets and liabilities of the bank based on the remaining period up to 31 December 2016 to the contractual maturity date.

Liquidity risk is addressed through the following measures:

- The bank enters into lending contracts subject to availability of funds.
- The bank has an aggressive strategy aimed at increasing the customer deposit base.
- The bank invests in short term liquid instruments which can easily be sold in the market when the need arises.
- Investments in equipment are properly budgeted for and done when the bank has sufficient cash flows.

The table below details the liquidity ratio trends over the year:

As at 31 December	2016 %	2015 %
Average for the period	41	52
Maximum for the period	43	57
Minimum for the period	39	42
Statutory minimum requirement by Central Bank of Kenya	20	20
	====	====

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

b) Liquidity risk (Continued)

Undiscounted cash flows

The table below shows the undiscounted cash outflows on the bank's financial liabilities based on their contractual maturity dates and the undiscounted cash inflows on the bank's financial assets based on their expected maturity dates. The banks expected cash flows on these instruments could vary significantly from this analysis. For example, demand deposits from customers are expected to maintain a stable or increasing balance; and unrecognised loan commitments are not all expected to be drawn down immediately

	Upto 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
As at 31 December 2016						
FINANCIAL ASSETS						
Cash and balances with CBK	758,326	-	-	-	-	758,326
Deposits and balances from banking institutions	215,173	-	-	-	-	215,173
Government securities	-	256,432	451,950	702,990	892,947	2,304,319
Other investments	-	-	46,662	80,302	-	126,964
Advances to customers	77,201	1,361,217	1,265,199	2,432,063	663,864	5,799,544
	1,050,700	1,617,649	1,763,811	3,215,355	1,556,811	10,366,306
FINANCIAL LIABILITIES						
Customer deposits	1,493,295	5,014,897	488,526	668,995	-	7,665,713
Amounts due to local banks	51,334	-	-	-	-	51,334
	1,544,629	5,014,897	488,526	668,995	-	7,717,047
Net liquidity gap	(493,929)	(3,397,248)	1,275,285	2,546,360	1,556,811	2,649,259
	=======	========	======	=======	========	=======
As at 31 December 2015						
Total financial assets	1,498,838	1,873,175	1,746,882	3,750,603	1,666,740	10,536,238
Total financial liabilities	2,651,481	5,571,138	542,712	743,199	-	9,508,530
Net liquidity gap	(1,152,643)	(3,697,963)	1,204,170	3,007,404	1,666,740	1,027,708
	========	========	=======	=======	========	=======

The gross nominal inflow/(outflow) disclosed is the contractual, undiscounted cash flow on the financial liability or commitment.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

c) Market Risk

(i) Interest rate risk

The bank is exposed to the risk that the value of a financial instrument will fluctuate due to changes in market interest rate. Interest rates on advances to customers are either pegged to the bank's base lending rate or Treasury bill rate.

The interest rates, therefore, fluctuate depending on the movement in the market interest rates. The bank also invests in fixed interest rate instruments issued by the Central Bank of Kenya. Interest rate on customer deposits is negotiated between the bank and the customer. The bank has the discretion to change the rates in line with changes in market trends.

The board of directors has assigned the authority for the management oversight of the interest rate risk policy to the Assets and Liability Committee (ALCO). The committee which is composed of the CEO, Treasury Manager, and other bank officers meets as necessary for specific credit risk situations, reviews various liquidity and funding decisions and related risks.

Formal minutes pertaining to committee actions are recorded and maintained for review by the board of directors.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

c) Market Risk (Continued)

(i) Interest rate risk (Continued)

The table below summarises the exposure to interest rate risks. Included in the table are the bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates. The bank does not bear an interest rate risk on off financial position items. All figures are in thousand of shillings.

	Up to 1 Month Sh '000	1-3 Months Sh '000	4-12 Months Sh '000	1-5 years Years Sh '000	Over 5 Years Sh '000	Non-interest Bearing Sh '000	Total Sh'000
FINANCIAL ASSETS							
Cash in hand	-	-	-	-	-	104,398	104,398
Balances with Central Bank of Kenya	-	-	-	-	-	653,928	653,928
Deposits and balances due from banking institutions	215,173	-	-	-	-	-	215,173
Government securities	-	49,373	136,052	473,704	1,645,190	-	2,304,319
Corporate bonds	-	-	-	114,445	-	-	114,445
Advances to customers	-	1,327,296	1,249,445	2,349,241	778,393	95,169	5,799,544
Total financial assets	215,173	1,376,669	1,385,497	2,937,390	2,423,583	853,495	9,191,807
FINANCIAL LIABILITIES							
Customer deposits	46,404	5,552,476	514,414	514,500	-	1,037,919	7,665,713
Amounts due to local banks	51,334	-	-	-	-	-	51,334
Total financial liabilities	97,738	5,552,476	514,414	514,500	-	1,037,919	7,717,047
Interest rate sensitivity gap	117,435	(4,175,807)	871,083	2,422,890	2,423,583	(184,424)	1,474,760
As at 31 December 2015							
Total financial assets	521,344	1,476,467	1,735,535	3,960,224	1,666,740	977,494	10,337,804
Total financial liabilities	1,497,999	5,433,534	492,792	493,328	-	1,033,491	8,951,144
Interest rate sensitivity gap	(976,655)	(3,957,067)	1,242,743	3,466,896	1,666,740	(55,997)	1,386,660

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the bank. It is unusual for a bank's interest to completely be matched due to the nature of business terms and types.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

c) Market Risk (Continued)

(i) Interest rate risk (Continued)

Exposure to interest rate risk

The bank is exposed to various risks associated with the effects of fluctuation in the prevailing levels of market interest rates on its financial position and cash flows. ALCO closely monitors the interest rate trends to minimize the potential adverse impact of interest rate changes. The table below summarises the exposure to interest rate risk at the statement of financial position date.

Interest rate risk – stress test-as at 31 December 2016

	Amount Sh'000	Scenario 10% increase in net margin Sh'000	Scenario 10% decrease in net margin Sh'000
Profit before taxation	104,665	120,669	88,660
Adjusted core capital	1,555,345	1,571,349	1,539,341
Adjusted total capital	1,637,829	1,653,833	1,621,825
Risk weighted assets (RWA)	5,973,616	5,973,616	5,973,616
Adjusted core capital to RWA	26%	26%	26%
Adjusted total capital to RWA	27%	28%	27%
	=======	=======	========

Interest rate risk – stress test-as at 31 December 2015

	Amount Sh'000	Scenario 10% Increase in net margin Sh'000	Scenario 10% Decrease in net margin Sh'000
Profit before taxation	168,204	234,654	103,099
Adjusted core capital	1,449,830	1,515,608	1,384,053
Adjusted total capital	1,531,527	1,597,305	1,465,750
Risk weighted assets (RWA)	6,349,081	6,349,081	6,349,081
Adjusted core capital to RWA	23%	24%	22%
Adjusted total capital to RWA	24%	25%	23%
	=======	=======	========

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

c) Market Risk (Continued)

ii) Foreign exchange risk (Continued)

Foreign exchange risk is the risk that may occur to earnings or capital that results from movement of foreign exchange rates. This type of risk affects the bank due to cross-border investing and operating activities. The board of directors has assigned authority for management oversight of the foreign exchange risk policy to the CEO and Treasury manager.

Management of foreign exchange risk

The bank operates wholly within Kenya and its assets and liabilities are reported in the local currency. The bank's currency risk is managed within the Central Bank of Kenya exposure guideline of 20% core capital. The bank's management monitors foreign currency exposure on a daily basis.

The bank's currency position is as follows:

	KES Sh '000	GBP Sh '000	USD Sh '000	EURO Sh '000	OTHERS Sh '000	Total Sh '000
At 31 December 2016						
FINANCIAL ASSETS						
Cash in hand	79,790	1,644	17,275	5,682	7	104,398
Balances with CBK	636,595	210	16,499	616	8	653,928
Deposits and balances due from banking institutions	56,267	40,497	55,787	52,283	3,248	208,082
Government securities	2,304,319	-	-	-	-	2,304,319
Other securities	114,445	-	-	-	-	114,445
Advances to customers	5,124,054	2,634	459,426	213,430	-	5,799,544
Other assets	113,325	29	-	12,322	-	125,676
Total financial assets	8,428,795	45,014	548,987	284,333	3,263	9,310,392
FINANCIAL LIABILITIES						
Customer deposits	7,058,394	46,082	501,462	61,964	-	7,667,902
Amounts due to local banks	-	-	51,334	-	-	51,334
Other Liabilities	(155,672)	(8)	(2,424)	221,590	-	63,486
Total financial liabilities	6,902,722	46,074	550,372	283,554	-	7,782,722
Net balance sheet position	1,526,073	(1,060)	(1,385)	779	3,263	1,527,670
At 31 December 2015						
Total financial assets	9,561,357	18,203	490,201	368,556	1,749	10,440,066
Total financial liabilities	8,094,943	18,325	668,616	189,415	-	8,971,299
Net balance sheet position	1,466,414	(122)	(178,415)	179,141	1,749	1,468,767

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

c) Market Risk (Continued)

ii) Foreign exchange risk (Continued)

The table below shows the foreign exchange risk sensitivity analysis. The net position is after a 10% increase or decrease in foreign currency exchange rates against the Kenya shilling.

At 31 December 2016

	Amount Sh'000	Scenario 10% increase in foreign currency rate Sh'000	Scenario 10% decrease in foreign currency rate Sh'000
Profit before taxation	104,665	85,507	123,822
Adjusted core capital	1,555,345	1,534,550	1,572,865
Adjusted total capital	1,637,829	1,617,034	1,655,349
Risk weighted assets (RWA)	5,973,616	5,973,616	5,973,616
Adjusted core capital to RWA	26%	26%	26%
Adjusted total capital to RWA	27%	27%	28%
	=======	=======	========

At 31 December 2015

	Amount Sh'000	Scenario 10% increase in foreign currency rate Sh'000	Scenario 10% decrease in foreign currency rate Sh'000
Profit before taxation	168,876	214,474	123,278
Adjusted core capital	1,449,830	1,495,428	1,404,232
Adjusted total capital	1,531,527	1,577,125	1,485,929
Risk weighted assets (RWA)	6,349,081	6,349,081	6,349,081
Adjusted core capital to RWA	23%	24%	22%
Adjusted total capital to RWA	24%	25%	23%
	=======	=======	========

iii) Price risk

Treasury bonds held at fair value are stated at their market value on the last day of business in the year .These are subject to frequent variations due to changes in their market prices.

An increase or decrease in rates by 10% with all other variables held constant, will have a decrease/increase in shareholders' equity of Sh 8,850,367 (2015: Sh 19,671,600).

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

d) Capital Management

Regulatory capital

The Central Bank of Kenya sets and monitors capital requirements for the bank.

The bank's objectives when managing capital are:

- To safeguard the bank'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 development needs of the business.
- To comply with the capital requirements set by the Central Bank of Kenya.

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

The Central Bank of Kenya requires each bank to:

a) Hold the minimum level of regulatory capital of Sh 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 8%;

c) Maintain a core capital of not less than 8% of total deposit liabilities and

d) Maintain total capital of not less than 12% of risk weighted assets plus risk weighted off financial position items.

In addition to the above minimum capital adequacy ratios of 8% and 12%, with effect from 1 January 2015, institutions are required to hold a capital conservation buffer of 2.5% over and above these minimum ratios to enable institutions withstand future periods of stress. This brings the minimum core capital to risk weighted assets and total capital to risk weighted assets requirements to 10.5% and 14.5% respectively. The capital conservation buffer is made up of high quality capital which should comprise mainly of common equity, premium reserves and retained earnings.

Institutions that currently meet the minimum capital ratios of 8% and 12% but remain below the buffer-enhanced ratios of 10% and 14.5% should maintain prudent earnings retention policies with a view to meeting the conservation buffer within 24 months effective from 1 January 2015.

The bank's regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes ordinary share capital, share premium, retained earnings, after deductions for intangible assets (excluding computer software), investments in equity instruments of other institutions and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.
- Tier 2 capital, which includes 25% revaluation surplus which have received prior CBK approval, qualifying subordinated liabilities and collective impairment allowances.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

iv) Capital Management (Continued)

The bank'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 bank 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 has complied with all externally imposed capital requirements throughout the period.

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

	Nominal financial position amounts		Risk weighted amounts	
ASSETS	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Cash (including foreign notes and coins)	104,398	73,166	-	-
Cash balances with Central Bank of Kenya	653,928	904,328	-	-
Government securities	2,304,319	2,896,653	-	-
Corporate bonds	114,445	155,701	-	-
Deposits and balances due from banking institutions	215,173	436,239	37,057	75,787
Loans and advances to customers	5,799,544	5,871,717	4,454,101	4,426,838
Other assets	125,676	99,007	125,676	99,007
Property and equipment	71,776	76,373	71,776	76,373
Intangible assets	13,874	4,572	13,874	4,572
Deferred tax asset	6,380	4,758	6,380	4,758
Tax recoverable	17,418	3,195	17,418	3,195
Total assets on balance sheet	9,426,931	10,525,709	4,726,282	4,690,530
Total asset off balance sheet	375,276	470,601	323,096	356,664
Total risk weighted assets	9,802,207	10,996,310	5,973,618	6,349,080
Tier 1 Capital	1,555,345	1,449,830		
Tier 1 + Tier 2 Capital	1,637,829	1,531,527		
Basel ratio				
Tier 1 (CBK minimum – 8%)	26%	23%		
Tier 1 + Tier 2 (CBK min – 12%)	27%	24%		

The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation, by Risk and Credit, and is subject to review by the Credit Committee or ALCO as appropriate.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

e) Operating risk

Non-financial risk management disclosures

The Board of Directors has put in place a framework for management of non-financial risk management of the bank. The Board Risk Management Committee (BMRC) is responsible for monitoring compliance of this framework with the bank's overall risk management policies and procedures, and review of the adequacy of the risk management framework in relations to non-financial risks faced by the bank.

The key non-financial risks the bank faces are strategic risk, operational risks, reputational risk, compliance/legal risk.

i) Strategic risk

Strategic risk is a function of the internal and the external environment. The strategic risk policy of the bank provides direction and guidance to the board of directors for anticipating change, both externally and internally.

The bank uses key indicators to measure strategic risk such as: Current and forecasted economic conditions such as economic growth, inflation, interest rates, foreign exchange trends and other useful key economic data such as demography and demographic structures; trends within the banking sector such as, Competition both from existing players and new entrants; Merger and acquisition activities; Changes in customer needs, wants and behaviour; development of new products and use of technology; Changes in the bank's various sector exposures and the associated risks; and achievement of the targets, goals and objectives set by the board.

Responsibilities of strategic risk

The board of directors is responsible for the formulation and overall implementation of the bank's strategy. Strategy execution, strategic risk planning and overall strategic risk management is delegated to managing director.

Management of strategic risk

The board and management use the board, committees, and strategic plan to manage strategic risk. Regular and adhoc meetings of the board, the board committees review reports of the management and take corrective action. The execution of the bank's 5 year strategic plan is a key tool for strategic risk with the current strategic plan being 2010-2016. The next strategic plan cycle plan is being developed.

ii) Bank operational risk

The bank's operational risk framework is designed to identify risks, measures and mitigate operational risks. These are risks associated with human error, system failures or technological failure, inadequate procedures and controls, unforeseen catastrophes, or other operational problems which may result in unexpected losses.

Responsibilities for operational risk management

The General Manager-Operations, continually reports to the Managing Director on all the key risks of the bank. Risk & Compliance department as well as Internal Audit reports both report to the managing director and their respective board committees.

Management of operational risk

Through use of key performance indicators (KPI's) so as to adequately reflect the key risk area, and report on them. KPI's are reported monthly, quarterly, or on emergencies, whichever is appropriate. An examples of a KPI is 'Incident/Fraud/ Suspicious Activities and Transaction Reports.'

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

e) Operating risk (Continued)

These detail those process related operational risk incidents combined with what remedial action was taken and what steps implemented to avoid a repeat occurrence. These reports are submitted as soon as the incident is discovered and notable trends reported quarterly on a summary report.

Reporting operational risk is a key part of risk management and staff are required to report all incidents which could fall within any of the six key risk areas (as above) – whether or not they resulted in any actual loss to the Bank.

iii) Reputational risk

Reputational risk is the potential that negative publicity may lead to decline of its customer base, costly litigation, revenue reduction and subsequently its value and brand. All other risks may lead to reputational risks.

Main source of reputational risks are: business viability, business practices, fraudulent activities, litigations, customer satisfaction, anti-money laundering (AML) and rumours.

Responsibilities for reputational risk

The responsibility for management of reputational risk lies with the board of directors of the bank. Nonetheless, risk and audit management committees are responsible for reviewing adequacy and effectiveness of internal control systems relating to reputation risk and means through which exposures related to reputation risk are managed. Their purpose is to ensure that all stakeholders meet the bank's reputational risk objectives.

Management of Reputational risk

Overall, the bank promotes a corporate culture that adequately addresses stakeholder concerns and result in a gain of confidence. Internally, the bank have developed a code of conduct for directors and senior management and all staff. The bank also fully complies with applicable laws, legislation, and regulations. Finally, we continually communicate to the staff and regulators and the public on our compliance and standards.

iv) Compliance (legal/regulatory) risk

Compliance risk refers to the potential of loss arising from non-compliance or violation of laws, rules, regulations, obligatory practices/standards, contractual agreements. The bank is variously exposed to compliance risk due to relations with a wide number of stakeholders, e.g. regulators, customers, counter parties, as well as tax authorities, local authorities and other authorized agencies. The bank meets high standards of compliance with the Central Bank of Kenya, County governments, Occupational Safety and Health Administration (OSHA) and National Environment Management Authority (NEMA) etc.

Management of regulatory and legal risk

The risk & compliance department identifies and monitors the key risks and is responsible for ensuring that the day to day business controls comply with applicable legislation and are in line with best practice. Internal and external legal counsel work closely with business units to identify areas of existing and potential regulatory/legal risks and actively manage them to reduce the bank's exposures.

The board risk management committee receive the risk & compliance department's report on the strength of the bank's compliance risk framework to enable them determine whether it is under control.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

e) Operating risk (Continued)

iv) Compliance (legal/regulatory) risk (Continued)

Management of regulatory risks

The board of directors and senior management through adoption of the bank's corporate governance and code of conduct sets a culture of integrity. All employees are required to attest to this code when they join the bank and thereafter annually, indicating that they have understood it and that they have complied with its provisions.

The bank has implemented compliance risk in key areas such as Know Your Customer (KYC) policy. Customer due diligence (CDD) and transactions monitoring has been ongoing. Cash transaction reporting (CTR) and Suspicious Account Transactions Reporting (SATR) is done as required by FRC. The risk and compliance department periodically update business units on the Anti Money Laundering's on UN Security Committees reports on individuals and entities who been place on travel ban and funds frozen and embargo on arms as well as other regional and national bodies involved in fighting Money Laundering and Combating terrorism including the FAFT 40 and the Wolfsberg-Private Banking Principles.

v) IT risk

The bank's information technology risk management ensures presence of an effective mechanism to identify, measure, monitor, and control the risks inherent in the banks' IT systems, ensure data integrity, availability, confidentiality and consistency and provide the relevant early warning mechanism.

Responsibilities for Management of IT Risk

The three key functions responsible are the board, senior management and IT Head. The board ensures there is an IT governance structure that meets its risk tolerance. Senior management ensures staff understands and adheres to IT Risk Management. The Head of IT is key in decision making on business development that require the use of IT and that such system meet the bank's needs.

Management of IT Risk

By restricted access to both the IT system and physical access to IT infrastructure(s), IT security deployment and periodic IT Audit.

3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

f) Fair value of financial assets and liabilities

The table below shows an analysis of financial instruments at fair value by level of the fair value hierarchy. The financial instruments are grouped into levels 1 to 3 based on the degree to which the fair value is observable.

i) Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
ii) Level 2 fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as a price) or indirectly (i.e. derived from prices);and
iii) Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs)

	Note	Level 1 Shs'000	Level 2 Shs'000	Level 3 Shs'000	Total Shs'000
31 December 2016					
Financial assets designated as available for sale					
Treasury bonds	15	91,294	-	-	91,294
		=======	=======	======	========
31 December 2015					
Financial assets designated at fair value through profit or loss					
Treasury bonds	15	1,543,167	-	-	1,543,167
		=======	=======	======	=======

The treasury bonds were valued at quoted bid prices in an active market (Nairobi Securities Exchange). The directors consider that the carrying amounts of financial assets and liabilities recognised in the statement of financial position approximate their fair values.

There were no transfers between levels 1, 2, and 3 in the period (2015: none).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. INTEREST INCOME

	Group		Bank	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Advances to customers	941,817	944,833	941,817	944,833
Government securities - Held to maturity	121,284	184,289	121,284	184,289
Government securities - At fair value through profit or loss and Available for sale	91,294	155,227	91,294	155,227
Corporate bonds - Held to maturity	15,561	19,882	15,561	19,882
Deposits/balances due from other financial institutions	12,052	36,752	12,052	36,752
	1,182,008	1,340,983	1,182,008	1,340,983

5. INTEREST EXPENSE

	Group		Bank	
Customer deposits	871,855	764,130	871,855	764,130
Deposits and balances due to banking institutions	14,466	20,640	14,466	20,640
	886,321	784,770	886,321	784,770

6. FEES AND COMMISSION INCOME

	Group		Bank	
Transaction related fees	34,157	45,720	31,207	43,960
Credit related fees and commissions	24,580	27,624	24,580	27,624
	58,737	73,344	55,787	71,584

7. GAIN ON FOREIGN EXCHANGE DEALINGS

Gains on foreign currency dealings arose from trading in foreign currency transactions and also on the translation of foreign currency assets and liabilities.

8. OTHER OPERATING INCOME

	Group 2016 Sh'000	Group 2015 Sh'000	Bank 2016 Sh'000	Bank 2015 Sh'000
Locker rental income	1,266	1,156	1,266	1,156
Other operating income	10,371	5,413	10,371	5,413
	11,637	6,569	11,637	6,569

9. OPERATING EXPENSES

	Group		Bank	
Staff costs (note 10)	137,762	124,619	135,683	122,219
Contribution to Deposit Protection Fund	12,230	11,349	12,230	11,349
Depreciation (note 20)	21,152	20,546	21,152	20,546
Amortisation of intangible assets (note 21)	1,555	1,604	1,525	1,574
Directors' emoluments	26,192	21,407	26,192	21,407
Auditors' remuneration	11,052	2,600	10,577	2,600
Rent and rates	32,848	43,509	32,848	43,509
Legal and professional fees	6,456	7,709	6,456	7,709
Insurance	5,420	4,732	5,420	4,732
Security	10,357	10,158	10,357	10,158
Telephone and postage	10,847	10,213	10,847	10,213
Repairs and maintenance	4,626	3,846	4,626	3,846
Commission expenses	438	309		
Other expenses	35,121	70,882	35,409	71,189
	316,056	333,483	313,322	331,051

10. STAFF COSTS

	Group 2016 Sh'000	Group 2015 Sh'000	Bank 2016 Sh'000	Bank 2015 Sh'000
Salaries and allowances	129,912	116,938	127,833	114,538
Staff training	259	1,223	259	1,223
Terminal dues	635	1,272	635	1,272
NSSF contributions	408	404	408	404
Pension contributions-defined contribution scheme	4,756	3,627	4,756	3,627
Leave pay expense	966	733	966	733
Medical expenses	826	422	826	422
	137,762	124,619	135,683	122,219

11. TAXATION

	Group		Bank	
(a) Taxation charge				
Current taxation based on the taxable profit for the period at 30%	-	12,930	-	12,930
Deferred taxation (credit)/charge (note 22):-				
- current year (credit)	(1,557)	(3,594)	(1,622)	(3,392)
- prior year under provision	-	1,313	-	1,313
	(1,557)	10,649	(1,622)	10,851

	Group		Bank	
(b) Reconciliation of taxation charge to the expected taxation based on profit before taxation				
Profit before taxation	104,882	168,204	104,666	168,876
Tax at the applicable rate of 30%	31,465	50,461	31,400	50,663
Effect of expenses disallowed for taxation purposes	35,839	13,205	35,839	13,205
Effect of income not subject to taxation	(68,861)	(54,330)	(68,861)	(54,330)
Prior year underprovision	-	1,313	-	1,313
Taxation charge	(1,557)	10,649	(1,622)	10,851

	Group		Bank	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
(c) Corporate tax recoverable				
At 1 January	3,230	16,125	3,195	16,125
Taxation charge	-	(12,930)	-	(12,930)
Tax paid in the year	14,223	(35)	14,223	-
At 31 December	17,453	3,230	17,418	3,195

12 . EARNINGS PER SHARE

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

	Group		Bank	
	2016	2015	2016	2015
Earnings				
Earnings for the year attributable to ordinary shareholders (Sh'000)	108,075	157,555	107,924	158,025
Number of shares				
Weighted average number of ordinary shares in issue	1,000,000	1,000,000	1,000,000	1,000,000
Earnings per share-Basic (Sh)				
Ordinary shares	108.08	157.55	107.92	158.03

The diluted earnings per share is the same as the basic earnings per share as there were no potentially dilutive shares as at 31 December 2016 or 31 December 2015 respectively.

13. CASH AND BALANCES WITH CENTRAL BANK OF KENYA

	Group		Bank	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Cash on hand	104,398	73,166	104,398	73,166
Balances with Central Bank of Kenya				
- Cash ratio requirement	402,565	394,542	402,565	394,542
- Deposits held under lien	10,240	10,230	10,240	10,230
- Current account with CBK	241,123	499,556	241,123	499,556
	653,928	904,328	653,928	904,328
	758,326	977,494	758,326	977,494

The cash ratio requirement is based on the customer deposits with the bank as adjusted by the Central Bank of Kenya requirements. As at 31 December 2016 the cash reserve ratio requirement was 5.25% (2015: 5.25%) of all customer deposits. The deposits held under lien are to support foreign currency clearing. These funds are not available for the day to day operations of the bank.

14. DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS

	Group		Bank	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Deposits due from banking institutions	50,800	132,780	50,800	132,780
Balances due from banking institutions	164,373	303,459	164,373	303,459
	215,173	436,239	215,173	436,239

The weighted average effective interest rate for deposits and balances due from banking institutions at 31 December 2016 was 8.5% (2015 – 8.5%).

MATURITY ANALYSIS OF DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS

	Group & Bank	
	2016 Sh'000	2015 Sh'000
Due on demand	50,800	132,780
Maturing within one month	164,373	303,459
	215,173	436,239

15. GOVERNMENT SECURITIES - Group and Bank

	Group & Bank	
	2016 Sh'000	2015 Sh'000
(a) **Treasury bills held to maturity**		
At amortized cost – maturing within 90 days		
Face value	150,000	200,000
Less: unearned discount	(7,003)	(1,566)
	142,997	198,434

	2016 Sh'000	2015 Sh'000
(b) Treasury bonds		
At fair value through profit or loss - maturing after 3 years	-	1,521,596
At Fair value – Available for sale – maturing after 3 years	91,636	-
Held to maturity – at amortised cost (maturing within 5 years)	1,361,337	761,924
Held to maturity – at amortised cost (maturing after 5 years)	708,349	414,699
	2,069,689	1,176,623
	2,304,319	2,896,653

(c) Movement in treasury bonds (at fair value through profit or loss) can be summarised as follows:

	2016 Shs'000	2015 Shs'000
At 1 January	1,521,596	1,543,167
Additions	5,839,700	749,457
Disposals	(7,258,308)	(635,782)
Losses from changes in fair value	-	(135,246)
Net gains on trading	(102,988)	-
At 31 December	-	1,521,596

The weighted average effective interest rate for treasury bonds as at 31 December 2016 was 11 % (2015 – 11%).Included in the above balances are treasury bonds amounting to Sh 130,000,000 (2015 – Sh 70,000,000) pledged with local commercial banks as security for letters of credit and guarantee facilities.

(d) Movement in treasury bonds (Available for sale) can be summarised as follows:

	Group & Bank	
	2016 Shs'000	2015 Shs'000
At 1 January	-	-
Additions	90,000	-
Disposals	-	-
Gains from changes in fair value	1,636	-
At 31 December	91,636	-

16. CORPORATE BONDS - Group and Bank

Held to maturity- at amortised cost		
Corporate bonds maturing within 5 years	114,445	155,701

The weighted average effective interest rate on the bonds at 31 December 2016 was 7% (2015 – 7%).

Movement in corporate bonds held to maturity can be summarised as follows:

	2016 Shs'000	2015 Shs'000
At 1 January	155,701	198,314
Redemption	(34,725)	(34,725)
Net amortisation	(6,531)	(7,888)
At 31 December	114,445	155,701

17. ADVANCES TO CUSTOMERS

	Group 2016 Sh'000	Group 2015 Sh'000	Bank 2016 Sh'000	Bank 2015 Sh'000
Loans and advances to customers	5,941,941	5,972,815	5,941,941	5,972,815
Bills discounted	2,594	2,594	2,594	2,594
	5,944,535	5,975,409	5,944,535	5,975,409
Provision for impaired loans and advances (note 18)	(144,991)	(103,692)	(144,991)	(103,692)
	5,799,544	5,871,717	5,799,544	5,871,717

The weighted average effective interest rate on advances to customers as at 31 December 2016 was 15.38% (2015 – 18.28%).

Included in net advances are loans and advances amounting to Sh 334,970,000 (2015 – Sh 201,199,000), net of specific provisions, which have been classified as non-performing.

Advances to related parties are disclosed in note 30.

	Group 2016 Sh'000	Group 2015 Sh'000	Bank 2016 Sh'000	Bank 2015 Sh'000
Analysis of gross advances by maturity:				
Maturing within one year	2,678,869	2,844,711	2,678,869	2,844,711
Over one year to three years	1,215,191	1,247,374	1,215,191	1,247,374
Over three to five years	2,050,475	1,883,324	2,050,475	1,883,324
	5,944,535	5,975,409	5,944,535	5,975,409

18. PROVISION FOR IMPAIRED LOANS AND ADVANCES

	Group 2016	Group 2015	Bank 2016	Bank 2015
At 1 January	103,692	172,099	103,692	172,099
Provisions in the year charged to profit or loss	60,333	12,345	60,333	12,345
Write offs	(19,034)	(80,752)	(19,034)	(80,752)
At 31 December	144,991	103,692	144,991	103,692

19. OTHER ASSETS

	Group 2016	Group 2015	Bank 2016	Bank 2015
Items in course of collection	15,052	8,874	15,052	8,874
Prepayments	64,521	51,435	64,521	51,435
Other receivables	46,752	40,041	45,103	37,698
	126,325	100,350	124,676	98,007

20. EQUIPMENT - Group and Bank

	Computers & office equipment Sh'000	Motor vehicles Sh'000	Furniture, fittings and office renovations Sh'000	Total Sh'000
COST				
At 1 January 2015	76,762	8,271	158,882	243,915
Additions	3,744	2,404	1,131	7,279
Disposal	-	(867)	-	(867)
At 31 December 2015	80,506	9,808	160,013	250,327
At 1 January 2016	80,506	9,808	160,013	250,327
Additions	8,387	725	7,443	16,555
At 31 December 2016	88,893	10,533	167,456	266,882
DEPRECIATION				
At 1 January 2015	55,229	5,593	93,454	154,275
Charge for the year	6,035	939	13,572	20,546
Disposal	-	(867)	-	(867)
At 31 December 2015	61,264	5,665	107,025	173,954
At 1 January 2016	61,264	5,665	107,025	173,954
Charge for the year	6,244	1,332	13,576	21,152
At 31 December 2016	67,508	6,997	120,602	195,106
NET BOOK VALUE				
At 31 December 2016	21,385	3,536	46,855	71,776
At 31 December 2015	19,242	4,143	52,988	76,373

Included in equipment are assets with a cost of Sh 128,908,362 (2015 - Sh 95,238,962) which were fully depreciated. The notional depreciation charge in respect of these assets for the year is Sh 20,975,227 (2015 – Sh 15,496,736).

21. INTANGIBLE ASSETS COMPUTER SOFTWARE

	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
COST				
At 1 January	32,262	31,768	32,113	31,768
Additions	10,827	494	10,827	345
At 31 December	43,089	32,262	42,940	32,113
AMORTISATION				
At 1 January	27,571	25,967	27,541	25,967
Charge for the year	1,555	1,604	1,525	1,574
At 31 December	29,126	27,571	29,066	27,541
NET BOOK VALUE				
At 31 December	13,963	4,691	13,874	4,572

22. DEFERRED TAXATION ASSET

	Group		Bank	
The deferred tax asset, computed at the enacted rate of 30%, is attributable to the following items:				
Accelerated capital allowances	4,645	3,458	4,645	3,458
Leave pay provision	1,630	1,300	1,630	1,300
Other provisions	596	-	596	-
Unrealised fair vaue gain on financial assets	(484)	-	(491)	-
Tax losses	130	202	-	-
	6,517	4,960	6,380	4,758
The movement on the deferred tax asset account is as follows:				
As at 1 January	4,960	2,679	4,758	2,679
Credit for the year – note 11(a)	1,557	3,594	1,622	3,392
Prior year underprovision - note 11(a)	-	(1,313)	-	(1,313)
At 31 December	6,517	4,960	6,380	4,758

23. INVESTMENT IN SUBSIDIARY – Bank

	No. of shares	Holding	2016 Sh'000	2015 Sh'000
Parabank Insurance Agency Limited	1,000	100%	1,000	1,000

The subsidiary is wholly owned Limited Liability Company incorporated and domiciled in Kenya. The company was incorporated on 22 May 2015 and licenced to operate Insurance Agency/ brokerage business. The principal activity of the company is insurance agency business.

24. CUSTOMER DEPOSITS

	Group		Bank	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Current accounts	540,283	1,031,586	542,472	1,033,491
Savings accounts	284,464	271,442	284,464	271,442
Call deposits	252,647	229,843	252,647	229,843
Fixed deposits	6,588,319	6,532,331	6,588,319	6,532,331
	7,665,713	8,065,202	7,667,902	8,067,107
Analysis of customer deposits by maturity:				
Payable within 90 days	6,635,474	6,344,329	6,637,663	6,346,234
Payable after 90 days and within one year	514,500	572,129	514,500	572,129
Payable after one year	515,739	1,148,744	515,739	1,148,744
	7,665,713	8,065,202	7,667,902	8,067,107

The weighted average effective interest rate on interest bearing customer deposits at 31 December 2016 was 12.25 % (2015 – 10.13%).

Customers deposits from related parties are disclosed in note 29 and concentrations of customer deposits are covered under note 3(a).

25. DEPOSITS AND BALANCES DUE TO BANKING INSTITUTIONS – Group & Bank

	2016 Sh'000	2015 Sh'000
Deposits due to banking institutions	51,334	884,037

The weighted average effective interest rate for deposits and balances due to banking institutions at 31 December 2016 was 5% (2015 – 12%).

26. OTHER LIABILITIES

	Group		Bank	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Sundry payables	40,089	20,156	40,089	20,156
Accruals	18,169	14,278	17,964	13,789
Premiums payable	3,213	3,585	-	-
Leave pay provision	5,433	4,335	5,433	4,335
	66,904	42,354	63,486	38,280

27. SHARE CAPITAL

	Group & Bank	
	2016 Sh'000	2015 Sh'000
Authorised, issued and fully paid		
1,000,000 ordinary shares of Sh 1,000 each	1,000,000	1,000,000

28. NOTES TO THE STATEMENT OF CASH FLOWS

(a) Reconciliation of profit before taxation to cash (used in)/generated from operations

	Group		Bank	
	2016 Sh '000	2015 Sh '000	2016 Sh '000	2015 Sh '000
Profit before taxation	104,882	168,204	104,666	168,876
Adjustments for:				
Depreciation	21,152	20,546	21,152	20,546
Amortization of intangible assets	1,555	1,604	1,525	1,574
Profit on sale of equipment	-	(400)	-	(400)
Fair value changes in treasury bonds	1,636		1,636	-
Working capital changes :	129,225	189,954	128,979	190,596
Increase in balances held by Central Bank of Kenya under lien	(10)	(1,160)	(10)	(1,160)
Decrease/(Increase) in advances to customers	72,173	(1,424,102)	72,173	(1,424,102)
Decrease in treasury bonds	592,334	931,905	592,334	931,905
Decrease in corporate bonds	41,256	42,613	41,256	42,613
(Decrease)/Increase in other assets	(25,975)	2,794	(26,669)	3,137
(Decrease)/Increase in customer deposits	(399,489)	17,190	(399,205)	19,095
(Decrease) in advances from other local banks	(832,703)	(52,206)	(832,703)	(52,206)
Increase/(Decrease) in other liabilities	24,550	2,553	25,206	(1,521)
Cash (used in) operations	(398,639)	(290,459)	(398,639)	(291,643)

28. NOTES TO THE STATEMENT OF CASH FLOWS (Continued)

	Group		Bank	
	2016 Sh '000	2015 Sh '000	2016 Sh '000	2015 Sh '000
(b) Analysis of balances of cash and cash equivalents as shown in the financial position and notes				
Cash on hand	104,398	73,166	104,398	73,166
Deposits and balances due from banking institutions	215,173	436,239	215,173	436,239
Current account with Central Bank of Kenya	643,688	894,098	643,688	894,098
	963,259	1,403,503	963,259	1,403,503

For the purposes of the statement of cash flows, cash equivalents include short term liquid investments which are readily convertible into known amounts of cash and which were within three months of maturity when acquired, less advances from banks repayable within three months from the dates of the advances.

29. CONTINGENCIES AND COMMITMENTS INCLUDING OFF FINANCIAL POSITION ITEMS

	2016 Sh'000	2015 Sh'000
(a) Contingent liabilities		
Letters of credit	92,782	183,572
Letters of guarantee and performance bonds	165,064	211,164
Bills for collection	117,430	75,865
	375,276	470,601

Letters of credit are commitments by the bank to make payments to third parties, on production of documents, on behalf of customers and are reimbursed by customers.

Letters of guarantee and performance bonds are issued by the bank, on behalf of customers, to guarantee performance by customers to third parties. The bank will only be required to meet these obligations in the event of default by the customers.

Contingent liabilities arising from law suits as at 31 December 2016 amounted to Sh 10,700,000 (2015- Sh 10,700,000)

(b) The bank had no capital commitments as at 31 December 2016 (2015 – Sh NIL).

(c) Commitments to extend credit

Commitments to lend are agreements to lend to a customer in future subject to certain conditions. Such commitments are normally made for a fixed period. The bank may withdraw without incurring any charges from its contractual obligation to extend credit by giving reasonable notice to the customer.

29. CONTINGENCIES AND COMMITMENTS INCLUDING OFF FINANCIAL POSITION ITEMS (Continued

d) Operating lease arrangements

The bank as a lessee

At the financial position date, the bank had outstanding commitments under operating leases which fall due as follows:

	2016 Sh'000	2015 Sh'000
Within one year	8,179	22,917
In the second to fifth year inclusive	32,782	31,630
	40,961	54,547

30. 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.

Placements at 31 December 2016 include placements made in the bank by directors, their associates and companies associated to directors. Advances to customers and deposits at 31 December 2016 include loans and advances to companies associated to directors employees of the bank and, also deposits held with related parties respectively. Contingent liabilities at 31 December 2016 include guarantees and letters of credit for companies associated to directors.

These balances are included in the loans and advances and deposits balances at year end.

	Directors' associated companies		Employees/staff	
	2016 Sh'000	2015 Sh'000	2016 Sh'000	2015 Sh'000
Movement in related party balances was as follows:				
Loans and advances:				
At 1 January	437,688	524,554	43,352	33,082
Net movement during the year	(104,836)	(86,866)	29,642	10,270
At 31 December	332,852	437,688	72,994	43,352
Interest earned	53,256	70,030	6,934	5,202
Deposits:				
At 1 January	348,633	271,454	11,409	8,741
Net movement during the year	37,116	77,179	5,565	2,668
At 31 December	385,749	348,633	16,974	11,409
Interest paid	38,575	34,863	1,358	913

30. RELATED PARTY TRANSACTIONS (Continued)

	2016 Sh'000	2015 Sh'000
Guarantees and letters of credit to companies associated to directors	30,834	10,392

Key management compensation

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

	2016 Sh'000	2015 Sh'000
Key management salaries and other benefits	63,409	57,536
Directors emoluments	26,192	21,407

The remuneration of directors and key executives is determined by the board of directors having regard to the performance of the individuals and market trends.

31. FAIR VALUE

The directors consider that there is no material difference between the fair value and carrying value of the company's financial assets and liabilities where fair value details have not been presented.

32. FIDUCIARY ACTIVITIES

At 31 December 2016, the bank did not hold asset security documents on behalf of customers (2015: none).

33. COUNTRY OF INCORPORATION

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

34. CURRENCY

The financial statements are presented in Kenya Shillings thousands (Sh'000), the bank's functional and presentation currency.

35. EVENTS AFTER REPORTING PERIOD

There are no significant events after the reporting period which has been reported in these financial statements.

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