PARAMOUNT BANK

UKAS ENVIRONMENTAL MANAGEMENT 005

CERTIFICATION DE SYSTÈME ISO 9001 SGS

ANNUAL REPORT & FINANCIAL STATEMENTS 2020

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BRANCH NETWORK

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Our Strategic Framework

Aim

Our aim is to achieve and sustain a reputation for quality by offering banking products and services that exceed the requirements of our customers. We strive to remain the bank of first choice in all our product and services.

Vision

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

Mission

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

Awards & Accolades

At the most recent Think Business Banking Awards 2020, Paramount Bank were awarded the 'Best Bank in Tier IV' and '2nd Runner Up for Bank with Lowest Charges'! Winners are chosen by an independent judging panel and include all commercial banks in Kenya.

Best Bank in Tier IV – Think Business Banking Awards 2020

2nd Runner Up Bank with Lowest Charges – Think Business Banking Awards 2020

Corporate Social Responsibility

Introduction

In the year 2020, Paramount Bank diversified it's CSR programs with a regional spread approach across the country. The bank has committed all its resources available towards these programs in making sure they are conducted and monitored in the most efficient manner. The staffs, board of directors and management have all participated and continue to do so, in order to make a positive impact in the community and the country as a whole. Through their involvement they are able to understand the financial lives of their consumers and using that insight to develop affordable, innovative and scalable products to help them improve their financial health. The two main projects conducted this year were the #GoingGreen Campaign, which touched many environmental issues and the Makongeni SDA Church outreach program.

#GoingGreen Campaign

Eldoret City Marathon Sponsors – Theme: 'Climate Action'

The Bank engages in environmental protection initiatives such as supporting the annual Eldoret City marathon which is a climate action campaign whose target is to plant/distribute 1 million tree seedlings in partnership with the Kenya Forest Service, learning institutions, and the Eldoret City Marathon sponsors and partners. Launched in 2018, the marathon also aims to launch the careers of young, upcoming running talents. The City Marathon serves as a platform to create recognition for these young talents giving them national prominence without the need of a manager or agent.

Paramount Bank through its Eldoret Branch, has been sponsoring the Eldoret City Marathons in liaison with the County Government of Uasin Gishu since its inception back in 2018. Due to the ongoing Covid-19 Pandemic, the marathon did not happen but instead a tree planting ceremony was held.
As a way to conserve the environment and continue with our corporate social responsibility, the Bank participated in the tree planting campaign that was held at Kapseret forest, Simat/Kapseret Ward, Kapseret Sub-County by the County Government of Uasin Gishu and the Eldoret City Marathon.

The event was themed as 'Climate Action', which saw over 10,000 trees planted to mark the 2020's edition of the annual City Marathon. During the campaign, a number of Government officials were in attendance advising the people on the importance of conserving the environment through planting more trees giving a target of 15% forest cover by the year 2022 from the current stand which is at 10% forest cover.

Park Rehabilitation

Paramount Bank carried out a tree-planting programme at a park whose community has continuously been supported by the Bank over the years. Our efforts showed immense results in giving back to the community through rehabilitation of a recreational park where the land was illegally grabbed and recently recovered by the residents.

The Bank contributed towards a tree planting campaign to rehabilitate the park, working together with students of the International School of Kenya. Due to the on-going pandemic, the tree planting campaign was put on hold. The rehabilitation of the park aimed at enhancing community development, creating a safe and secure environment for the area residents.

Corporate Social Responsibility
(Continued)

Environmentally Friendly Business

As part of the Going Green Campaign, Paramount Bank advocates for its suppliers to hold the same environmentally friendly values that the bank holds through educative material on energy use, greenhouse gas emissions, water and hazardous waste. Plans to create a policy on funding environmentally friendly investments and investors are underway, this will see the Bank embrace the environmental, social and governance factors.

The Bank is gearing towards generating a positive environmental impact through the creation of a campaign, which will see the bank go paperless through automating the customer delivery process. The process involves, identifying the crucial points that would require human contact and automating those that do not require human interaction, this will enable us to reduce the paperwork and trim the branch footprint.

Makongeni SDA Church Outreach Program

To achieve balance of our economic, environmental, and social practices, in line with our shareholder expectations, Paramount Bank has engaged in voluntary social integration with the Makongeni SDA (Seventh Day Adventist) Church.

The Makongeni SDA Church is located in Makongeni Estate, Jogoo Road (Nairobi, Kenya). The Church has a membership of about 500 people consisting of middle to low-level income members. The leadership includes a Church Pastor and 10 elders who facilitate the day-to-day running of the Church.
The Church has a football team known as Makongeni SDA Football Club, which has 30 football players who are non-Adventists. The football club was created by the church to rehabilitate the Youth who reside around the church. The football club gives them a sense of belonging and through the programme, the Church can teach them the values and impact their lives positively.

Paramount Bank donated 3 sets of branded uniforms with both the Paramount and Makongeni SDA FC logos. The Bank also donated 2 balls to the team.

The programme was carried out around the Christmas period, the Bank provided Christmas hampers to the 30 football team members.

The Paramount Bank hosted a team building activity at Mysa and included a few of the football team members of the Makongeni SDA Football Club. The Bank donated football kits at Mysa. They also held a football tournament where the Paramount Bank Football Club Participated as well as the Makongeni SDA Football Club. After the tournament, the Bank held a dinner at the Mc Frys Restaurant, Gigiri for the players.

With the on-going Covid-19 pandemic, several members of the church lost their jobs. The Church produced a committee who would facilitate ways to assist the church members. The committee would oversee the process through which the members would be supported. Paramount Bank contributed 100 bales of flour towards the initiative to assist and support the members.

Corporate Information

DIRECTORS	Anwarali Padany	- Chairman
	Ayaz Merali	- Cheif Executive Officer (CEO)
	Noorez Padamshi	
	Muhammad Mujtaba	- (Retired 30th June 2020)
	Mercy Kamau	
	Eunice Wamaitha	
AUDIT COMMITTEE	Eunice Wamaitha	- Chairperson
	Noorez Padamshi	
	Mercy Kamau	
	Henry Onkunya	
CREDIT COMMITTEE	Mercy Kamau	- Chairperson
	Eunice Wamaitha	
	Anwarali Padany	
	Ayaz Merali	
	Muhammad Mujtaba	- (Retired 30th June 2020)
ASSET LIABILITY COMMITTEE	Ayaz Merali	- Chairperson
	Nicholas Odera	
	Muhammad Mujtaba	- (Retired 30th June 2020)
	Fred Maina	
	Kapil Deo Sharma	
RISK MANAGEMENT COMMITTEE	Eunice Wamaitha	- Chairperson
	Anwarali Padany	
	Noorez Padamshi	
	Deluxe Atanga	
BOARD NOMINATIONS AND REMUNERATION COMMITTEE	Anwarali Padany	- Chairperson
	Noorez Padamshi	
	Eunice Wamaitha	
COMPANY SECRETARY	Winniefred Nyagoha Jumba Certified Public Secretary (Kenya) C/o Coulson Harney LLP - Bowmans 5th Floor, West Wing, ICEA Lion Centre Riverside Park, Chiromo Road, Nairobi P.O.Box 10643 Nairobi, GPO 00100	

Corporate Information
(Continued)

REGISTERED OFFICE	LR Plot No 1870/IX/140 4th Floor, Sound Plaza Woodvale Groove P.O.Box 14001- 00800 Nairobi, Westlands
AUDITORS	Deloitte & Touche Certified Public Accountants (Kenya) Deloitte Place, Waiyaki Way, Muthangari P.O.Box 40092 Nairobi, GPO 00100
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
PRINCIPAL CORRESPONDENTS	Standard Bank of South Africa, Johannesburg HDFC Bank, India BMCE, Spain Crown Agents Bank, UK

Report Of The Directors

The directors submit their report together with the audited financial statements for the year ended 31 December 2020, in accordance with Section 653(1) of the Kenyan Companies Act, 2015, which discloses the state of affairs of Paramount Bank Limited (the "Group and the Bank").

INCORPORATION

The bank and its subsidiary, Parabank Insurance Agency Limited, are both incorporated in the Republic of Kenya under the Companies Act, 2015, 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 2020:

	GROUP		BANK	
	2020 Sh'000	2019 Sh'000	2020 Sh'000	2019 Sh'000
Profit before taxation	97,063	86,574	96,554	85,643
Taxation credit /(charge)	36,387	5,029	36,527	5,306
Profit for the year	133,450	91,603	133,081	90,949

BUSINESS REVIEW

The Bank

Paramount Bank Ltd began operations under the name Combined Finance Ltd in 1993. Our paid up capital was SHS 25m and the services offered were general deposits and minor personal lending. Over the years we have grown into a fully-fledged bank offering almost all services that are offered in the banking industry today. We have seven branches spread across major towns in the country. For more information on the bank please refer to the bank's website www.paramountbank.co.ke.

External Environment

The external environment remained challenging because of measures announced by the government to contain Covid -19. The measures whereas necessary, adversely affected business activity across the country. Lock downs imposed by the government which including closing schools, significant restrictions on travel and curfews etc adversely affected the business environment. The result of this was massive layoffs and business closures across the country. Indeed, this is not just a Kenyan but global challenge.

The government has since started gradually relaxing the containment measures and we expect the economic recovery to pick up pace as a result. We expect a sharp increase in economic activities in the year 2021.

There is of course a lot of concern about the sustainability of the government debt levels. There is already evidence that the government seems to be having a challenge serving its debts considering government revenues through taxes have not risen in tandem.

The macroeconomic environment however remained stable with inflation, interest rates and exchange rates remaining largely within acceptable limits.

The Bank's Performance

The Bank's performance remained stable. There has been an 8% increase in Net Interest Income from Sh 406m in the previous year to Sh 441m in the current year due to increased lending activities. Total operating income also increased by 19% from Sh. 466m in the previous year to Sh. 554m in the current year largely due to increased income from trade in government securities and non-interest income. There was a significant increase (7 times) in impairment losses on loans and advances as a result of increase in credit risk as a result of economic down arising on the impact of Covid 19. Overall the profit before tax increased 12% from Sh 86m in the previous year to Sh. 97 m in the current year

On the balance sheet side total assets grew by 9% from Sh. 10,443m in the previous year to Sh. 11,378m in the current year. There was a 27% increase in investment in government securities and a 6% increase in advances to customers as compared to the previous year. Customer deposits increased by 9% from Sh. 8.478m in the previous year to Sh. 9.265m in the current year. There was a 7% increase in shareholder funds from Sh. 1.778m in the previous year to Sh. 1,911m in the current year.

Overall the bank registered steady and stable results will all its core capital and liquidity ratios remaining strong.

Looking ahead

The outlook for 2021 seems favourable with an expected improvement in economic conditions considering that the government is gradually relaxing the Covid-19 containment measures. We expect the macroeconomic variables like interest rates, inflation, exchange rates etc to remain stable. We expect the GDP to grow by at least 5% to 6% mainly due to the continued heavy infrastructure led investment by the government, continued foreign investment in the country and improving general economy.

DIVIDENDS

The directors do not recommend the payment of a dividend in respect of the year ended 31 December 2020 (2019: Sh Nil).

DIRECTORS

The present members of the Board of Directors are shown on page 9.

DIRECTORS' STATEMENT AS TO INFORMATION GIVEN TO AUDITORS

Each of the persons who is a director at the date of approval of this report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Group's auditors are unaware; and
- the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Group's auditors are aware of that information.

AUDITORS

Deloitte & Touche, having expressed their willingness, continue in office in accordance provisions of section 719 (2) of the Kenyan Companies Act, 2015, and subject to approval by the Central Bank of Kenya in accordance with Section 24 of the Banking Act. The Directors monitor the effectiveness, objectivity and independence of the auditor. The Directors also approve the annual audit engagement contract, which sets out the terms of the auditor's appointment and the related fees.

BY ORDER OF THE
BOARD

WJumba

Winnie Fred Nyagoha
Jumba
Secretary
Nairobi, Kenya
25th March 2021

Chairman's Report

I am pleased to once again present the Annual Report and Financial Statements for the year 2020. On behalf of the Board of Directors, I would like to acknowledge the dedication and commitment of our staff, management team and most of all our esteemed clients during these uncertain times. The bank adapted to the evolving economic environment made worse by the Covid-19 pandemic containment measures through quick adjustments and actions taken to ensure that the business remains resilient and responsive to customers.

Despite the impact of the Covid-19 pandemic to the economy, the bank continued to gradually expand its client and deposit base, which resulted in an increase in profits by over 45% in the year 2020 compared to 2019. In addition to growth in the balance sheet, the bank's liquidity position remains sufficient and adequate in meeting client needs. The bank experienced its highest growth rate in terms of total assets in the past 5 years at 9%, further exemplifying its resilient position during this period.

Paramount Bank emerged winners for the 'Best Bank in Tier IV' and 2nd Runners Up Overall for the 'Bank with the Lowest Charges for SMEs' in the latest Think Business Banking Awards. The Board of Directors would like to thank all its partners for their endless support, and ensures that the bank continues to pursue its vision to be regarded as one of the best banks in Kenya with the highest quality products and services to its customers.

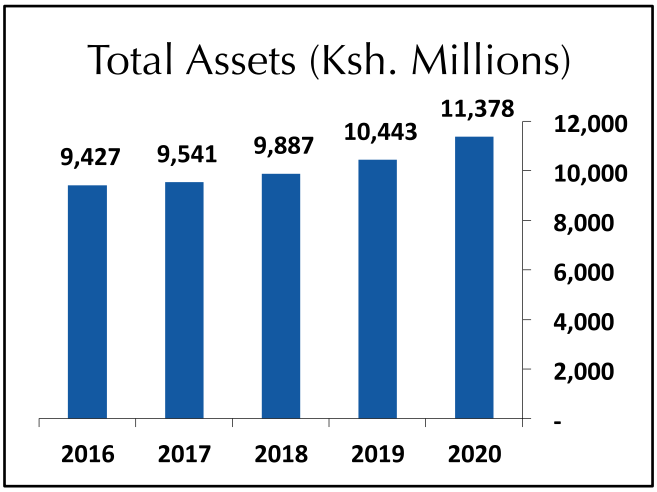
The bank made significant upgrades to all its digital banking platforms (Mobile and Internet Banking), in order to encourage and promote cashless banking as well as convenience to its customers. The banks website was redesigned, in order to provide an informative medium of communication to all its current and prospective customers.

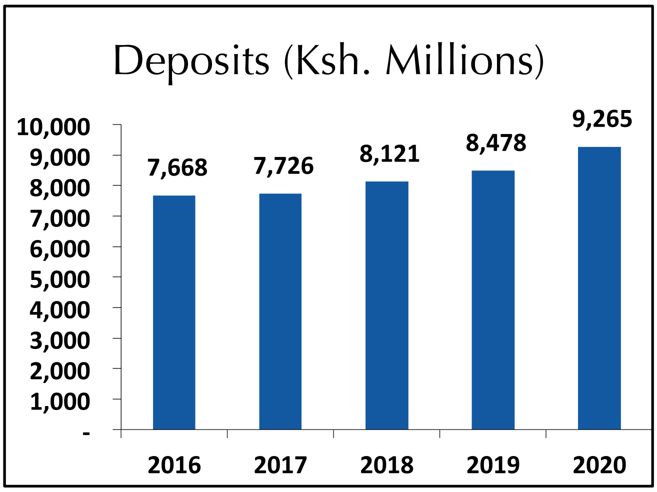
The Board would like to reassure all clients of its focus and commitment in keeping the bank strong during these challenging times. We appreciate all our stakeholders' continuous support, trust and commitment as the bank joins other Kenyans in rebuilding the economy and taking advantage of the emerging opportunities. We anticipate a strong rebound in 2021.

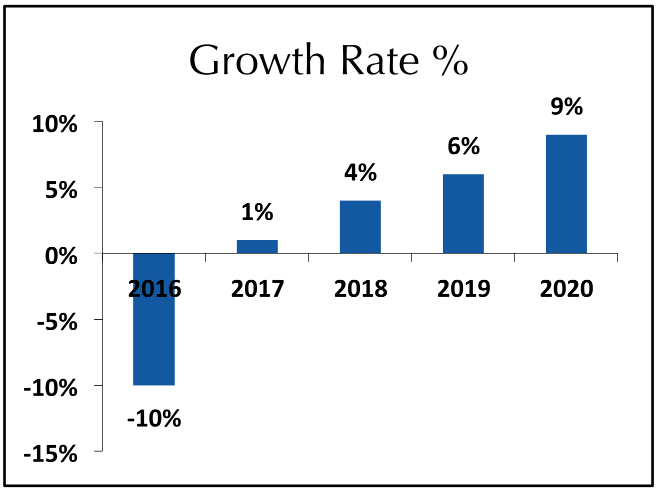
Thank You,

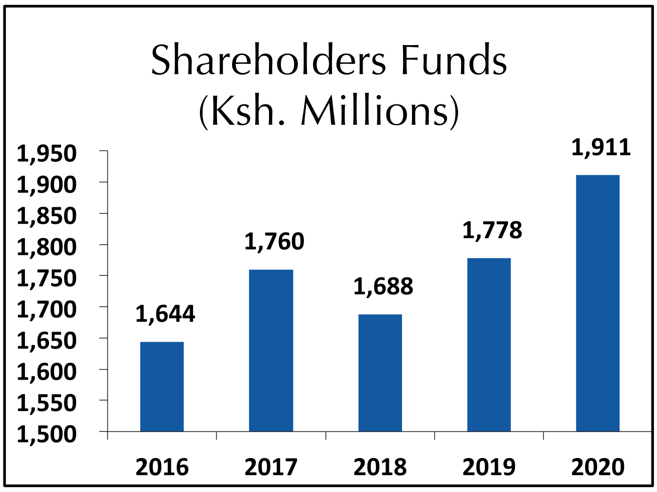
Anwarali Padany
Chairman
Paramount Bank Limited

Graphic Report

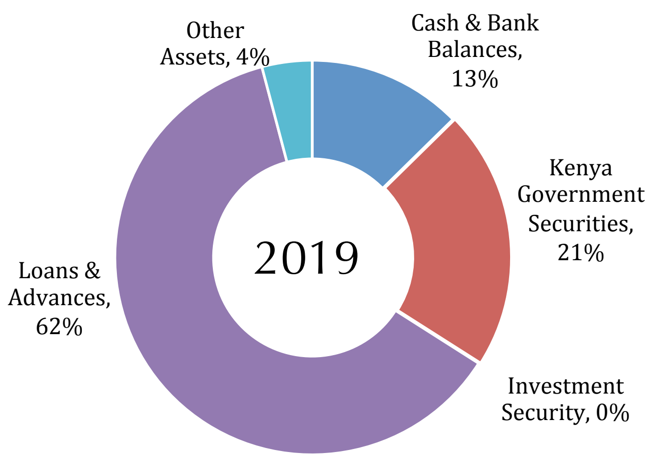


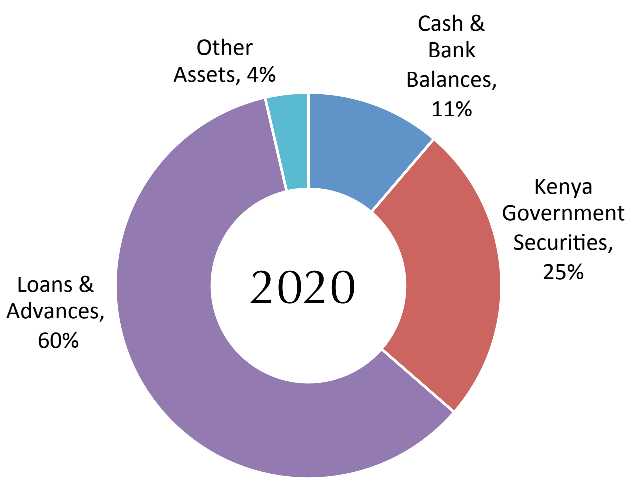






Asset Distribution





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 2020**
Anwarali Padany (Chairman)	4
Ayaz Merali	4
Noorez Padamshi	4
Muhammad Mujtaba	2
Mercy Kamau	4
Eunice Wamaitha	4

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. Directors' emoluments are shown in note 31.

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.

STATEMENT ON CORPORATE GOVERNANCE (Continued)

Committees of the Board (Continued)

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).

Anwarali Padany - Director
25th March 2021

Ayaz Merali - Director

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 company as at the end of the financial year and of its profit or loss for that year. It also requires the directors to ensure that the company maintains proper accounting records that are sufficient to show and explain the transactions of the company and disclose, with reasonable accuracy, the financial position of the company. The directors are also responsible for safeguarding the assets of the company, and for taking reasonable steps for the prevention and detection of fraud and error.

The directors accept responsibility for the preparation and presentation of these financial statements in accordance with the International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. 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 company's ability to continue as a going concern, the directors are not aware of any material uncertainties related to events or conditions that may cast doubt upon the company's ability to continue as a going concern.

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

Approved by the board of directors on **25th March** 2021 and signed on its behalf by:

Anwarali Padany - Director

Ayaz Merali - Director

Deloitte.

Deloitte & Touche Certified Public Accountants (Kenya)
Deloitte Place, Waiyaki way, Muthangari
P.O.Box 400092 – GPO 00100 Nairobi, Kenya

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

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

INDEPENDENT AUDITORS' REPORT
TO THE MEMBERS OF PARAMOUNT BANK LIMITED

Report on the Audit of the Financial Statements

Opinion

We have audited the accompanying financial statements of Paramount Bank Limited (the "Bank") and its subsidiary (together the "Group") set out on pages 12 to 81, which comprise the consolidated and bank statements of financial position as at 31 December 2020, and the consolidated and bank statements of profit or loss and other comprehensive income, the consolidated and bank statements of changes in equity and the consolidated and bank statements of cash flows for the year then ended, and the notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Group and Bank as at 31 December 2020 and of their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act, 2015.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("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 Group 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. 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, 2015 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.

Report on the Audit of the Financial Statements (Continued)

Responsibilities of the Directors for the Financial Statements (Continued)

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.

INDEPENDENT AUDITORS' REPORT
TO THE MEMBERS OF PARAMOUNT BANK LIMITED (Continued)

Report on the Audit of the Financial Statements (Continued)

Auditor's Responsibilities for the Audit of the Financial Statements (Continued)

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.

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

In our opinion, the information given in the Report of the Directors on pages 10 to 11 is consistent with the financial statements.

Deloitte & Touche

Certified Public Accountants (Kenya)

Nairobi **26th March 2021**

CPA Charles Munkonge Luo, Practising certificate No. 2294
Signing partner responsible for the independent audit

CONSOLIDATED AND BANK STATEMENTS OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2020

		GROUP		BANK	
		2020	2019	2020	2019
	Note	Sh'000	Sh'000	Sh'000	Sh'000
INTEREST INCOME	4	1,113,752	1,039,665	1,113,752	1,039,665
INTEREST EXPENSE	5	(672,799)	(633,320)	(672,799)	(633,320)
NET INTEREST INCOME		440,953	406,345	440,953	406,345
Fees and commission income	6	79,490	66,684	75,541	62,895
Gains on foreign exchange dealings	7	3,095	8,930	3,095	8,930
Other operating income/(loss)	8	34,426	(11,975)	34,426	(11,975)
OPERATING INCOME		557,964	469,984	554,015	466,195
Operating expenses	9	(352,736)	(371,089)	(349,296)	(368,231)
Impairment losses on loans and advances	18 (b)	(108,165)	(12,321)	(108,165)	(12,321)
PROFIT BEFORE TAXATION		97,063	86,574	96,554	85,643
TAXATION CREDIT	11(a)	36,387	5,029	36,527	5,306
PROFIT FOR THE YEAR		133,450	91,603	133,081	90,949
OTHER COMPREHENSIVE INCOME		-	-	-	-
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		133,450	91,603	133,081	90,949
		======	======	======	======
			Sh		Sh
EARNINGS PER SHARE – Basic and diluted	12	133.45	91.60	133.08	90.95
		=====	=====	=====	=====

CONSOLIDATED AND BANK STATEMENTS OF FINANCIAL POSITION
AS AT 31 DECEMBER 2020

		GROUP		BANK	
		2020	2019	2020	2019
	Note	Sh'000	Sh'000	Sh'000	Sh'000
ASSETS					
Cash and balances with Central Bank of Kenya	13	753,170	887,159	753,170	887,159
Deposits and balances due from banking institutions	14	528,121	433,658	528,121	433,658
Government securities	15	2,829,031	2,231,232	2,829,031	2,231,232
Right of use asset	16	88,308	112,088	88,308	112,088
Advances to customers (net)	17	6,827,408	6,462,963	6,827,408	6,462,963
Other assets	19	138,589	127,093	130,856	127,365
Corporate tax recoverable	11(c)	17,633	17,455	17,418	17,418
Equipment	20	33,823	45,261	33,823	45,261
Intangible assets	21	5,903	7,450	5,842	7,324
Deferred taxation asset	22	154,341	117,833	154,354	117,827
Investment in subsidiary	23	-	-	10,000	1,000
TOTAL ASSETS		11,376,327	10,442,192	11,378,331	10,443,295
LIABILITIES					
Customer deposits	24	9,257,964	8,472,835	9,265,434	8,478,884
Other liabilities	25	106,070	71,214	102,205	67,500
Lease Liability Obligation	26	99,394	118,694	99,394	118,694
TOTAL LIABILITIES		9,463,428	8,662,743	9,467,033	8,665,078
SHAREHOLDERS' FUNDS					
Share capital	27	1,000,000	1,000,000	1,000,000	1,000,000
Retained earnings		912,899	779,449	911,298	778,217
TOTAL SHAREHOLDERS' FUNDS		1,912,899	1,779,449	1,911,298	1,778,217
TOTAL SHAREHOLDERS' FUNDS AND LIABILITIES		11,376,327	10,442,192	11,378,331	10,443,295

The financial statements on pages 20 to 87 were approved and authorised for issue by the board of directors on March 2021 and were signed on its behalf by:

Anwarali Padany - Director

Noorez Padamshi - Director

Ayaz Merali - Chief Executive Officer

Winnie Fred Jumba - Company Secretary

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

	Share Capital Sh'000	Retained Earnings Sh'000	Statutory Reserve* Sh'000	Fair value Reserve Sh'000	Total Sh'000
At 1 January 2020	1,000,000	687,846	-	-	1,687,846
Total comprehensive income for the year	-	91,603	-	-	91,603
At 31 December 2020	1,000,000	779,449	-	-	1,779,449
	=======	======	=======	=======	=======
At 1 January 2020	1,000,000	779,449	-	-	1,779,449
Total comprehensive income for the year	-	133,450	-	-	133,450
At 31 December 2020	1,000,000	912,899	-	-	1,912,899
	=======	======	=======	=======	=======

*The statutory reserve represents an appropriation from retained earnings in compliance with Central Bank of Kenya 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 IFRS 9. The statutory reserve is not distributable.

Retained earnings relate to the cumulative earnings from operations and are distributable.

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

	Share Capital Sh'000	Retained Earnings Sh'000	Statutory Reserve* Sh'000	Fair value Reserve Sh'000	Total Sh'000
At 1 January 2019	1,000,000	687,268	-	-	1,687,268
Total comprehensive income for the year	-	90,949	-	-	90,949
Transfer to statutory reserve	-	-	-	-	-
At 31 December 2019	1,000,000	778,217	-	-	1,778,217
At 1 January 2020	1,000,000	778,217	-	-	1,778,217
Total comprehensive income for the year	-	133,081	-	-	133,081
At 31 December 2020	1,000,000	911,298	-	-	1,911,298

*The statutory reserve represents an appropriation from retained earnings in compliance with Central Bank of Kenya 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 IFRS 9. The statutory reserve is not distributable.

Retained earnings relate to the cumulative earnings from operations and are distributable.

CONSOLIDATED AND BANK STATEMENTS OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2020

		GROUP		BANK	
		2020	2019	2020	2019
	Note	Sh'000	Sh'000	Sh'000	Sh'000
CASH FLOWS FROM OPERATING ACTIVITIES					
Cash (used in)/generated from operations	28(a)	(6,787)	25,630	1,914	25,316
Tax paid during the year	11(c)	(299)	(257)	-	-
Net cash (used in)/generated from operating activities		(7,086)	25,373	1,914	25,316
CASH FLOWS FROM INVESTING ACTIVITIES					
Purchase of equipment	20	(4,656)	(5,710)	(4,656)	(5,710)
Purchase of intangible assets	21	(1,524)	(57)	(1,524)	-
Proceeds from sale of motor vehicle		500	15	500	15
Investment in subsidiary		-	-	(9,000)	-
Net cash used in investing activities		(5,680)	(5,752)	(14,680)	(5,695)
CASH FLOWS FROM FINANCING ACTIVITIES					
Payment of lease liabilities	26	(27,550)	(26,838)	(27,550)	(26,838)
Net cash used in financing activities		(27,550)	(26,838)	(27,550)	(26,838)
(DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS		(40,316)	(7,217)	(40,316)	(7,217)
CASH AND CASH EQUIVALENTS AT 1 JANUARY		1,310,682	1,317,899	1,310,682	1,317,899
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	28(b)	1,270,366	1,310,682	1,270,366	1,310,682
		=======	=======	=======	=======

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2020

1 ACCOUNTING POLICIES

Statement of compliance

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

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.

Application of new and revised International Financial Reporting Standards (IFRSs)

i) New and amended IFRS Standards that are effective for the current year ended 31 December 2020

Several new and revised standards and interpretations became effective during the year. The Directors have evaluated the impact of their new standards and interpretations and none of them had a significant impact on the Group's financial statements.

The following revised IFRSs were effective in the current year and the nature and the impact of the relevant amendments are described below.

Covid-19-Related Rent Concessions Amendment to IFRS 16

In May 2020, the IASB issued Covid-19-Related Rent Concessions (Amendment to IFRS 16) that provides practical relief to lessees in accounting for rent concessions occurring as a direct consequence of COVID-19, by introducing a practical expedient to IFRS 16. The practical expedient permits a lessee to elect not to assess whether a COVID-19-related rent concession is a lease modification. A lessee that makes this election shall account for any change in lease payments resulting from the COVID-19-related rent concession the same way it would account for the change applying IFRS 16 if the change were not a lease modification.

The practical expedient applies only to rent concessions occurring as a direct consequence of COVID-19 and only if all of the following conditions are met:

a) The change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change;

b) Any reduction in lease payments affects only payments originally due on or before 30 June 2021 (a rent concession meets this condition if it results in reduced lease payments on or before 30 June 2021 and increased lease payments that extend beyond 30 June 2021); and

c) There is no substantive change to other terms and conditions of the lease

In the current financial year, the Group has not applied the practical expedient included in the amendment to IFRS 16 (as issued by the IASB in May 2020). There were no Covid-19 related rent concessions.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 ACCOUNTING POLICIES (Continued)

Application of new and revised International Financial Reporting Standards (IFRSs) (continued)

i) *New and amended IFRS Standards that are effective for the current year ended 31 December 2020 (continued)*

Amendments to References to the Conceptual Framework in IFRS Standards

The Group has adopted the amendments included in Amendments to References to the Conceptual Framework in IFRS Standards for the first time in the current year. The amendments include consequential amendments to affected Standards so that they refer to the new Framework. Not all amendments, however, update those pronouncements with regard to references to and quotes from the Framework so that they refer to the revised Conceptual Framework. Some pronouncements are only updated to indicate which version of the Framework they are referencing to (the IASC Framework adopted by the IASB in 2001, the IASB Framework of 2010, or the new revised Framework of 2018) or to indicate that definitions in the Standard have not been updated with the new definitions developed in the revised Conceptual Framework.

The Standards which are amended are IFRS 2, IFRS 3, IFRS 6, IFRS 14, IAS 1, IAS 8, IAS 34, IAS 37, IAS 38, IFRIC 12, IFRIC 19, IFRIC 20, IFRIC 22, and SIC-32. The adoption of the amendments has not had any material impact on the disclosures or on the amounts reported in these financial statements.

Amendments to IAS 1 and IAS 8 Definition of material

The Group has adopted the amendments to IAS 1 and IAS 8 for the first time in the current year. The amendments make the definition of material in IAS 1 easier to understand and are not intended to alter the underlying concept of materiality in IFRS Standards. The concept of 'obscuring' material information with immaterial information has been included as part of the new definition.

The threshold for materiality influencing users has been changed from 'could influence' to 'could reasonably be expected to influence'. The definition of material in IAS 8 has been replaced by a reference to the definition of material in IAS 1. In addition, the IASB amended other Standards and the Conceptual Framework that contain a definition of 'material' or refer to the term 'material' to ensure consistency.

The adoption of the amendments has not had any material impact on the disclosures or on the amounts reported in these financial statements.

ii) *Impact of new and amended standards and interpretations in issue but not yet effective*

At the date of authorization of these financial statements, the Group has not yet applied the following new and revised IFRS Standards that have been issued but are not yet effective.

IFRS 17	***Insurance Contracts***
IFRS 10 and IAS 28 (amendments)	*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*
Amendments to IAS 1	*Classification of Liabilities as Current or Non-current*
Amendments to IFRS 3	*Reference to Conceptual Framework*
Amendments to IAS 16	*Property, Plant and Equipment – Proceeds before Intended Use*
Amendments to IAS 37	*Onerous Contracts – Cost of Fulfilling a Contract*
Annual Improvements to IFRS Standards 2018 – 2020 Cycle	*Amendments to IFRS 1 First-time Adoption of International Financial Reporting Standards, IFRS 9 Financial Instruments, IFRS 16 Leases, and IAS 41 Agriculture*

The directors do not expect that the adoption of the Standards listed above will have a material impact on the financial statements of the Group in future periods.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 ACCOUNTING POLICIES (Continued)

iii) Early adoption of standards

The Group did not early-adopt any new or amended standards in the year ended 31 December 2020.

(a) 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.

(b) 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 ACCOUNTING POLICIES (Continued)

b) Basis of consolidation (Continued)

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.

c) 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.

(d) 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 drawdown 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.

(e) Net trading income

Net trading income arises from the margins that 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.

1 ACCOUNTING POLICIES (Continued)

(f) 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%
	=====

(g) 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.

(h) 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 ACCOUNTING POLICIES (Continued)

(i) 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.

(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.

1 ACCOUNTING POLICIES (Continued)

(j) 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.

(k) 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.

(l) Statutory reserve

IIFRS 9 requires the bank to recognise an impairment loss if there is expected losses on loans and receivables. However, Central Bank of Kenya prudential guidelines require the bank to set aside amounts for impairment losses on loans and advances in addition to those losses that have been recognised under IFRS 9. Any such amounts set aside represent appropriations of retained earnings and not expenses in determining profit or loss. These amounts are dealt with in the statutory reserve.

(m) Financial instruments

The Group applies IFRS 9 Financial Instruments to the recognition, classification and measurement, and derecognition of financial assets and financial liabilities and the impairment of financial assets.

Recognition

The Group recognises financial assets and liabilities when it becomes a party to the terms of the contract. Trade date or settlement date accounting is applied depending on the classification of the financial asset.

Classification and measurement

Financial assets are classified on the basis of two criteria:

i) the business model within which financial assets are managed, and
ii) their contractual cash flow characteristics (whether the cash flows represent 'solely payments of principal and interest' (SPPI)).

The Group assesses the business model criteria at a portfolio level. Information that is considered in determining the applicable business model includes (i) policies and objectives for the relevant portfolio, (ii) how the performance and risks of the portfolio are managed, evaluated and reported to management, and (iii) the frequency, volume and timing of sales in prior periods, sales expectation for future periods, and the reasons for such sales.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 ACCOUNTING POLICIES (Continued)

(m) Financial instruments (Continued)

The contractual cash flow characteristics of financial assets are assessed with reference to whether the cash flows represent SPPI. In assessing whether contractual cash flows are SPPI compliant, interest is defined as consideration primarily for the time value of money and the credit risk of the principal outstanding. The time value of money is defined as the element of interest that provides consideration only for the passage of time and not consideration for other risks or costs associated with holding the financial asset. Terms that could change the contractual cash flows so that it would not meet the condition for SPPI are considered, including: (i) contingent and leverage features, (ii) non-recourse arrangements and (iii) features that could modify the time value of money.

Financial assets will be measured at amortised cost if they are held within a business model whose objective is to hold financial assets in order to collect contractual cash flows, and their contractual cash flows represent SPPI.

Financial assets will be measured at fair value through other comprehensive income if they are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and their contractual cash flows represent SPPI.

Other financial assets are measured at fair value through profit and loss. There is an option to make an irrevocable election on initial recognition for non traded equity investments to be measured at fair value through other comprehensive income, in which case dividends are recognised in profit or loss, but gains or losses are not reclassified to profit or loss upon derecognition, and impairment is not recognised in the income statement.

Accounting for loans and advances and deposits held at amortised cost

Loans and advances to customers and banks, customer accounts and most financial liabilities are held at amortised cost. That is, the initial fair value (which is normally the amount advanced or borrowed) is adjusted for repayments and the amortisation of coupon, fees and expenses to represent the effective interest rate of the asset or liability. Balances deferred on-balance sheet as effective interest rate adjustments are amortised to interest income over the life of the financial instrument to which they relate. Financial assets that are held in a business model to collect the contractual cash flows and that contain contractual terms that give rise on specified dates to cash flows that are SPPI, are measured at amortised cost. The carrying value of these financial assets at initial recognition includes any directly attributable transaction costs.

In determining whether the business model is a 'hold to collect' model, the objective of the business model must be to hold the financial asset to collect contractual cash flows rather than holding the financial asset for trading or short-term profit taking purposes. While the objective of the business model must be to hold the financial asset to collect contractual cash flows this does not mean the Group is required to hold the financial assets until maturity. When determining if the business model objective is to collect contractual cash flows the Group will consider past sales and expectations about future sales.

(i) Significant increase in credit risk

In assessing whether the credit risk on a financial instrument has increased significantly since initial recognition, the Bank compares the risk of a default occurring on the financial instrument at the reporting date with the risk of a default occurring on the financial instrument at the date of initial recognition.

1 ACCOUNTING POLICIES (Continued)

(m) Financial instruments (Continued)

(i) Significant increase in credit risk (Continued)

In making this assessment, the Group considers both quantitative and qualitative information that is reasonable and supportable, including historical experience and forward-looking information that is available without undue cost or effort. Forward-looking information considered includes the future prospects of the industries in which the Banks's borrowers operate, obtained from economic expert reports, financial analysts, governmental bodies, relevant think-tanks and other similar organisations, as well as consideration of various external sources of actual and forecast economic information that relate to the Group's core operations.

In particular, the following information is taken into account when assessing whether credit risk has increased significantly since initial recognition:

- an actual or expected significant deterioration in the financial instrument's external (if available) or internal credit rating;
- significant deterioration in external market indicators of credit risk for a particular financial instrument, e.g. a significant increase in the credit spread, the credit default swap prices for the debtor, or the length of time or the extent to which the fair value of a financial asset has been less than its amortised cost;
- existing or forecast adverse changes in business, financial or economic conditions that are expected to cause a significant decrease in the debtor's ability to meet its debt obligations;
- an actual or expected significant deterioration in the operating results of the borrower;
- significant increases in credit risk on other financial instruments of the same borrower;
- an actual or expected significant adverse change in the regulatory, economic, or technological environment of the borrower that results in a significant decrease in the borrower's ability to meet its debt obligations.

Irrespective of the outcome of the above assessment, the Bank presumes that the credit risk on a financial asset has increased significantly since initial recognition when contractual payments are more than 30 days past due, unless the Bank has reasonable and supportable information that demonstrates otherwise.

Despite the foregoing, the Bank assumes that the credit risk on a financial instrument has not increased significantly since initial recognition if the financial instrument is determined to have low credit risk at the reporting date. A financial instrument is determined to have low credit risk if:

- The financial instrument has a low risk of default,
- The borrower has a strong capacity to meet its contractual cash flow obligations in the near term,
- Adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil its contractual cash flow obligations.

The Bank considers a financial asset to have low credit risk when the asset has external credit rating of 'investment grade' in accordance with the globally understood definition or if an external rating is not available, the asset has an internal rating of 'performing'. Performing means that the counterparty has a strong financial position and there is no past due amounts.

1 ACCOUNTING POLICIES (Continued)

(m) Financial instruments (Continued)

(ii) Definition of default

The Bank considers the following as constituting an event of default for internal credit risk management purposes as historical experience indicates that financial assets that meet either of the following criteria are generally not recoverable:

- when there is a breach of financial covenants by the borrower; or
- information developed internally or obtained from external sources indicates that the borrower is unlikely to pay its lenders and or creditors, including the Bank, in full (without taking into account any collateral held by the Bank).

Irrespective of the above analysis, the Bank considers that default has occurred when a financial asset is more than 90 days past due unless the Bank has reasonable and supportable information to demonstrate that a more lagging default criterion is more appropriate.

(iii) Credit-impaired financial assets

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

a) significant financial difficulty of the issuer or the borrower;
b) a breach of contract, such as a default or past due event (see (ii) above);
c) the lender(s) of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession(s) that the lender(s) would not otherwise consider;
d) it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
e) the disappearance of an active market for that financial asset because of financial difficulties.

(iv) Write-off policy

The Bank writes off a financial asset when there is information indicating that the borrower is in severe financial difficulty and there is no realistic prospect of recovery, e.g. when the borrower has been placed under liquidation or has entered into bankruptcy proceedings, or, when the amounts are over two years past due, whichever occurs sooner. Financial assets written off may still be subject to enforcement activities under the Bank's recovery procedures, taking into account legal advice where appropriate. Any recoveries made are recognised in profit or loss.

(v) Measurement and recognition of expected credit losses

The measurement of expected credit losses is a function of the probability of default, loss given default (i.e. the magnitude of the loss if there is a default) and the exposure at default. The assessment of the probability of default and loss given default is based on historical data adjusted by forward-looking information as described above. As for the exposure at default, for financial assets, this is represented by the assets' gross carrying amount at the reporting date; for financial guarantee contracts, the exposure includes the amount drawn down as at the reporting date, together with any additional amounts expected to be drawn down in the future by default date determined based on historical trend, the Bank's understanding of the specific future financing needs of the borrower, and other relevant forward-looking information.

1 ACCOUNTING POLICIES (Continued)

(m) Financial instruments (Continued)

(v) Measurement and recognition of expected credit losses (Continued)

For financial assets, the expected credit loss is estimated as the difference between all contractual cash flows that are due to the Bank in accordance with the contract and all the cash flows that the Bank expects to receive, discounted at the original effective interest rate.

If the Bank has measured the loss allowance for a financial instrument at an amount equal to lifetime ECL in the previous reporting period, but determines at the current reporting date that the conditions for lifetime ECL are no longer met, the Bank measures the loss allowance at an amount equal to 12-month ECL at the current reporting date.

Derecognition of financial assets

The Bank derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Bank retains substantially all the risks and rewards of ownership of a transferred financial asset, the Bank continues to recognise the financial asset and recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset measured at amortised cost, the difference between the asset's carrying amount and the sum of the consideration received and receivable is recognised in profit or loss. In addition, on derecognition of an investment in a debt instrument classified as at FVTOCI, the cumulative gain or loss previously accumulated in the investments revaluation reserve is reclassified to profit or loss. In contrast, on derecognition of an investment in equity instrument, which the Bank has elected on initial recognition to measure at FVTOCI, the cumulative gain or loss previously accumulated in the investments revaluation reserve is not reclassified to profit or loss, but is transferred to retained earnings.

Financial liabilities

After initial recognition, the company measures all financial liabilities including customer deposits, cash collaterals 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 company 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.

Borrowings

Borrowings are recorded at the proceeds received. Finance charges, including premiums payable on settlement or redemption, are accounted for on the accruals basis and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

1 ACCOUNTING POLICIES (Continued)

(m) Financial instruments (Continued)

Offsetting financial instruments

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

(n) 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.

(o) Leases

The Group assesses whether a contract is or contains a lease at inception of the contract. The Group recognises a right of use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets. For these leases, the Group recognises the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which the economic benefits from the leased assets are consumed.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted by using the rate implicit in the lease. If this rate cannot be readily determined, the Group uses its incremental borrowing rate.

Lease payments included in the measurement of the lease liability comprises of fixed lease payments (including the substance fixed payments), less any lease incentives.

The lease liability is presented as a separate line in the statement of financial position. The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method and by reducing the carrying amount to reflect the lease payments made.

The Group re-measures the lease liability (and makes a corresponding adjustment to the related right-of-use asset) whenever:

- the lease term has changed or there is a change in the assessment of exercise of a purchase option, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.
- the lease payments change due to changes in an index or rate or a change in expected payment under a guaranteed residual value, in which cases the lease liability is remeasured by discounting the revised lease payments using the initial discount rate (unless the lease payments change is due to a change in floating interest rate, in which case a revised discount rate is used).
- a lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 ACCOUNTING POLICIES (Continued)

(o) Leases (Continued)

The Group did not make any such adjustments during the periods presented.

The right-of-use assets comprise the initial measurement of the corresponding lease liability, lease payments made at or before the commencement day and any initial direct costs. They are subsequently measured at cost less accumulated depreciation and impairment loses.

Right-of-use assets are depreciated over the shorter period of lease term and useful life of the underlying asset. If a lease transfers ownership of the underlying asset or the cost of the right-of-use asset reflects that the Group expects to exercise a purchase option, the related right-of-use asset is depreciated over the useful life of the underlying asset. The depreciation starts at the commencement date of the lease.

The right-of-use assets are presented as a separate line in the statement of financial position.

The Group applies IAS 36 to determine whether a right-of-use asset is impaired and accounts for any identified impairment loss as described in the 'Property, plant and equipment' policy.

Variable rents that do not depend on an index or rate are not included in the measurement of the lease liability and the right-of-use asset. The related payments are recognised as an expense in the period in which the event or condition that triggers those payments occurs and are included in the line 'Other expenses' in the statement of the profit or loss.

(p) 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.

(q) 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.

(r) 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.

1 ACCOUNTING POLICIES (Continued)

(r) Employee benefit costs (Continued)

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.

(s) 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 entity'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 accounting judgements in applying the company's policies

Business model assessment

Classification and measurement of financial assets depends on the results of the SPPI and the business model test. The Bank determines the business model at a level that reflects how groups of financial assets are managed together to achieve a particular business objective. This assessment includes judgement reflecting all relevant evidence including how the performance of the assets is evaluated and their performance measured, the risks that affect the performance of the assets and how these are managed and how the managers of the assets are compensated. The Bank monitors financial assets measured at amortised cost that are derecognised prior to their maturity to understand the reason for their disposal and whether the reasons are consistent with the objective of the business for which the asset was held. Monitoring is part of the Bank's continuous assessment of whether the business model for which the remaining financial assets are held continues to be appropriate and if it is not appropriate whether there has been a change in business model and so a prospective change to the classification of those assets. No such changes were required during the periods presented.

Significant increase in credit risk

As explained in note 1, ECL are measured as an allowance equal to 12-month ECL for stage 1 assets, or lifetime ECL for stage 2 or stage 3 assets. An asset moves to stage 2 when its credit risk has increased significantly since initial recognition. IFRS 9 does not define what constitutes a significant increase in credit risk. In assessing whether the credit risk of an asset has significantly increased, the Bank takes into account qualitative and quantitative reasonable and supportable forward-looking information.

Establishing groups of assets with similar credit risk characteristics

When ECLs are measured on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics.

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

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

Establishing groups of assets with similar credit risk characteristics (Continued)

The Bank monitors the appropriateness of the credit risk characteristics on an on-going basis to assess whether they continue to be similar. This is required in order to ensure that should credit risk characteristics change there is appropriate re-segmentation of the assets. This may result in new portfolios being created or assets moving to an existing portfolio that better reflects the similar credit risk characteristics of that group of assets. Re-segmentation of portfolios and movement between portfolios is more common when there is a significant increase in credit risk (or when that significant increase reverses) and so assets move from 12-month to lifetime ECLs, or vice versa, but it can also occur within portfolios that continue to be measured on the same basis of 12-month or lifetime ECLs but the amount of ECL changes because the credit risk of the portfolios differ.

Models and assumptions used

The Bank uses various models and assumptions in estimating ECL. Judgement is applied in identifying the most appropriate model for each type of asset, as well as for determining the assumptions used in these models, including assumptions that relate to key drivers of credit risk.

ii) Key sources of estimation uncertainty

Establishing the number and relative weightings of forward-looking scenarios for each type of product and determining the forward-looking information relevant to each scenario:

When measuring ECL the Bank uses reasonable and supportable forward-looking information, which is based on assumptions for the future movement of different economic drivers and how these drivers will affect each other.

Probability of default:

PD constitutes a key input in measuring ECL. PD is an estimate of the likelihood of default over a given time horizon, the calculation of which includes historical data, assumptions and expectations of future conditions.

Loss Given Default:

LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, taking into account cash flows from collateral and integral credit enhancements.

Property and equipment

Critical estimates are made by the directors in determining depreciation rates for property and equipment.

Fair value measurement and valuation

Some of the company's assets and liabilities are measured at fair value for financial reporting process. In estimating the fair value of an asset or liabilities, the company uses market – observable data to the extent it is available. Where level 1 inputs are not available, the company engages third party qualified valuers to perform the valuation.

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

ii) Key sources of estimation uncertainty (Continued)

Key sources of estimation uncertainty in the application of IFRS 16 include the following:

- Determination of the appropriate rate to discount the lease payments; and
- Assessment of whether a right-of-use asset is impaired.

3 FINANCIAL RISK MANAGEMENT

This note presents information about the Bank's exposure to financial risks and the Bank's management of capital.

The Bank has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risks

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.

i) Credit quality analysis

An analysis of the Group's credit risk exposure per class of financial asset, internal rating and "stage" without taking into account the effects of any collateral or other credit enhancements is provided in the following tables. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

Explanation of the terms 'Stage 1', 'Stage 2' and 'Stage 3' is included in Note 3A(iii).

	Year ended 2020				
Loans and advances to customers at amortised cost	**Stage 1 12-month ECL Shs**	**Stage 2 Lifetime ECL Shs**	**Stage 3 Lifetime ECL Shs**	**Total Shs**	**Year ended 2019 Total Shs**
Grade 1: Normal	5,500,035			5,500,035	5,206,470
Grade 2: Watch	-	1,037,029	-	1,037,029	903,227
Grade 3: Substandard	-	-	457,946	457,946	470,030
Grade 4: Doubtful	-	-	313,464	313,464	312,902
Grade 5: Loss	-	-	-	-	-
Total gross carrying amount	**5,500,035**	**1,037,029**	**771,410**	**7,308,473**	**6,892,629**
Loss allowance	(160,063)	(84,857)	(236,146)	(481,065)	(429,666)
Carrying amount	**5,339,972**	**952,172**	**535,264**	**6,827,408**	**6,462,963**

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

i) Credit quality analysis (Continued)

The following table sets out information about the overdue status of loans and advances to customers in Stages 1, 2 and 3.

	2020				2019
In thousands Kenya Shillings	Stage 1	Stage 2	Stage 3	**Total**	**Total**
Loans and advances to customers at amortised cost – net carrying amount					
Current	5,339,972			5,339,972	5,107,645
Overdue < 30 days		952,172		952,172	804,813
Overdue > 90 days			535,264	535,264	539,694
Total	**5,339,972**	**952,172**	**535,264**	**6,827,408**	**6,462,963**

Cash and cash equivalents

The Bank held cash and cash equivalents of Shs 1,270 million at 31 December 2020 (2019: Shs 1,310 million). The cash and cash equivalents are held with central banks and financial institution counterparties that are rated at least B to AA+, based on Moody's ratings.

ii) Collateral held and other credit enhancements

The Bank holds collateral and other credit enhancements against certain of its credit exposures. The following table sets out the principal types of collateral held against different types of financial assets.

Type of credit exposure

	Percentage of exposure that is subject to collateral requirements		
In thousands Kenya Shillings	**31 December 2020**	**31 December 2019**	**Principal type of collateral held**
Loans and advances to customers	1,302,887	1,236,975	Cash deposit
Loans and advances to customers	4,623,583	4,398,080	Property discounted forced sale value
Loans and advances to customers	514,337	494,203	Debenture (50% of registered value)
Loans and advances to customers	386,598	333,705	Others
	6,827,408	6,462,963	

The Following table stratifies credit exposures from mortgage loans and advances to customers by ranges of loan-to-value (LTV) ratio. LTV is calculated as the ratio of the gross amount of the loan – or the amount committed for loan commitments – to the value of the collateral.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

ii) Collateral held and other credit enhancements (Continued)

The valuation of the collateral excludes any adjustments for obtaining and selling the collateral. For credit-impaired loans the value of collateral is based on the most recent appraisals.

In thousands Kenya Shillings	**31 December 2020**	**31 December 2019**
LTV ratio		
Less than 50%	1,117,480	1,190,669
51–70%	247,405	470,952
71–90%	1,167,049	530,941
91–100%	1,397,245	613,240
More than 100%	2,358,274	3,106,657
Total	6,287,453	5,912,459
Credit-impaired loans		
Less than 50%	25,345	7,664
51–70%	10,632	-
More than 70%	503,978	542,840
Total	539,955	550,504
Total	**6,827,408**	**6,462,963**

Loans and advances to corporate customers

The general creditworthiness of customers tends to be the most relevant indicator of credit quality of a loan extended to it. However, collateral provides additional security and the Bank generally requests that corporate borrowers provide it. The Bank may take collateral in the form of a first charge over real estate, floating charges over all corporate assets and other liens and guarantees.

Because of the Bank's focus on corporate customers' creditworthiness, the Bank does not routinely update the valuation of collateral held against all loans to corporate customers. Valuation of collateral is updated when the loan is put on a watch list and the loan is monitored more closely. For credit-impaired loans, the Bank obtains appraisals of collateral because it provides input into determining the management credit risk actions.

At 31 December 2020, the gross carrying amount of credit-impaired loans and advances to customers amounted to Shs 1,345 million (2019: Shs 1,263 million) and the value of identifiable collateral (mainly commercial properties) held against those loans and advances amounted to Shs 596 million (2019: Shs 611 million). For each loan, the value of disclosed collateral is capped at the nominal amount of the loan that it is held against.

Other types of collateral and credit enhancements

The Bank does not hold any other types of collateral and credit enhancements, such as second charges and floating charges for which specific values are not generally available.

The Bank has not obtained any assets by taking possession of collateral.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL

Inputs, assumptions and techniques used for estimating impairment

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Bank's historical experience and expert credit assessment and including forward-looking information.

The objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure (adjusted where relevant for changes in prepayment expectations).

The Bank uses three criteria for determining whether there has been a significant increase in credit risk:

- quantitative test based on movement in PD;
- qualitative indicators; and
- a backstop of 30 days past due

Credit risk grades

The Bank allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 2 and 3.

Each exposure is allocated to a credit risk grade on initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. The monitoring typically involves use of the following data.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Corporate exposures	Retail exposures	All exposures
– Information obtained during periodic review of customer files –e.g. audited financial statements, management accounts, budgets and projections. Examples of areas of particular focus are: gross profit margins, financial leverage ratios, debt service coverage, compliance with covenants, quality of management, senior management changes – Data from credit reference agencies, press articles, changes in external credit ratings – Actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities	– Internally collected data on customer behaviour – e.g. utilisation of credit card facilities – Affordability metrics – External data from credit reference agencies, including industry-standard credit scores	– Payment record – this includes overdue status as well as a range of variables about payment ratios – Utilisation of the granted limit – Requests for and granting of forbearance – Existing and forecast changes in business, financial and economic conditions

- The table below provides an indicative mapping of how the Bank's internal credit risk grades relate to PD and to external credit ratings of Moody's.
- The customer loans portfolio of the Bank comprises ordinary loans, business loans, current account loans, credit cards and bank guarantees.

Grading	12-month weighted-average PD	External rating
Grades 1: Normal	15%	AAA to B
Grades 2: Watch	45%	B- to C
Grades 3–5: Substandard and Doubtful	100%	Default

Inputs, assumptions and techniques used for estimating impairment

Significant increase in credit risk

Generating the term structure of PD

The Bank collects sector wise performance and default information about its credit risk exposures analysed by type of product and borrower. For some portfolios e.g government securities, information purchased from external credit reference agencies is also used.
The Bank employs statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

The method of PD parameter estimation is based on the ratio of PD = Gross Non-Performing Loan/Net Loans. The total gross GDP is projected from the previous year gross GDP using the GDP projection. The gross GDP per sector is then obtained by taking the ratio of the gross GDP per sector for the previous year and the total gross GDP for the previous year and multiplying that by the total gross GDP for the current year. The gross loans per sector is obtained by taking the ratio of the gross loans per sector for the previous year and the gross GDP per sector for the previous year and multiplying that by the gross GDP per sector for the current year.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Significant increase in credit risk (Continued)

The gross NPLs are projected using the regression coefficients for each of the sector. A regression is run on the gross NPLs against gross GDP for each of the sectors. The Bank uses one approach of generating PDs for all the loan portfolios.

Determining whether credit risk has increased significantly

The Bank assesses whether credit risk has increased significantly since initial recognition at each reporting date. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower, and the sectorial information.

The Bank considers credit risk of a particular exposure to have increased significantly since initial recognition based on a loan being rated as "watch". The Credit Committee reviews the loans periodically and the movement in the probability of default (PD) between the reporting period and initial recognition date of the loan to determine whether there has been a significant increase in credit risk.

Lifetime PDs are estimated considering the contractual maturities of exposures and estimated prepayment rates.

The credit risk may also be deemed to have increased significantly since initial recognition based on qualitative factors linked to the Bank's credit risk management processes that may not otherwise be fully reflected in its quantitative analysis on a timely basis. This will be the case for exposures that meet certain heightened risk criteria, such as placement on a watch list. Such qualitative factors are based on its expert judgment and relevant historical experiences.

For an explanation of the relevant qualitative indicators used for determining whether there has been a significant increase in credit risk, see Note 1 (m)(i).

As a backstop, the Bank considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

If there is evidence that there is no longer a significant increase in credit risk relative to initial recognition, then the loss allowance on an instrument returns to being measured as 12-month ECL. Some qualitative indicators of an increase in credit risk, such as delinquency or forbearance, may be indicative of an increased risk of default that persists after the indicator itself has ceased to exist. In these cases, the Bank determines a three months' probation period during which the financial asset is required to demonstrate good behaviour to provide evidence that its credit risk has declined sufficiently. When contractual terms of a loan have been modified, evidence that the criteria for recognising lifetime ECL are no longer met includes a history of up-to-date payment performance against the modified contractual terms.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Significant increase in credit risk (Continued)

Determining whether credit risk has increased significantly (Continued)

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- the criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- the criteria do not align with the point in time when an asset becomes 30 days past due;
- the average time between the identification of a significant increase in credit risk and default appears reasonable;
- exposures are not generally transferred directly from 12-month ECL measurement to credit- impaired; and
- there is no unwarranted volatility in loss allowance from transfers between 12-month PD (Stage 1) and lifetime PD (Stage 2).

Definition of default

The Bank considers a financial asset to be in default when:
- the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held);
- the borrower is more than 90 days past due on any material credit obligation to the Bank.
- Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than the current amount outstanding; or
- it is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to the borrower's inability to pay its credit obligations.
- In assessing whether a borrower is in default, the Bank considers indicators that are:
- qualitative: e.g. breaches of covenant;
- quantitative: e.g. overdue status and non-payment on another obligation of the same issuer to the Bank; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.
The definition of default largely aligns with that applied by the Bank for regulatory capital purposes.

Incorporation of forward-looking information

The Bank incorporates forward-looking information into both the assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and the measurement of ECL.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Incorporation of forward-looking information (Continued)

The base case is aligned with information used by the Bank for other purposes such as strategic planning and budgeting. External information considered includes economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Bank operates, supranational organisations such as the International Monetary Fund and selected private sector and academic forecasters.

Periodically, the Bank carries out stress testing of more extreme shocks to calibrate its determination of the upside and downside representative scenarios. A comprehensive review is performed at least annually on the design of the scenarios by a panel of experts that advises the Bank's senior management.

The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses.

The key drivers for credit risk is GDP growth, which generally incorporates other, indicates such as inflation, exchange rates etc. Another importance source of information used is the sector wise or industry wise total loans and advances and non-performing loans and advances as experienced by the banking industry. The Central Bank of Kenya publishes this information annually. The exposures are classified sector wise and credit losses computed for each sector individually.

The economic scenarios used as at 31 December 2020 included the following key indicators for Kenya for the years ending 31 December 2020 to 2023.

	Scenario	**2020**	**2021**	**2022**	**2023**	**2024**
GDP Growth rate	Base Case	1.50%	5.00%	4.00%	5.5%	5.5%
GDP Growth rate	Best Case	1.80%	6.00%	4.80%	6.60%	6.60%
GDP Growth rate	Worst Case	1.20%	4.00%	3.20%	4.40%	4.40%

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Incorporation of forward-looking information (Continued)

12 Months Probability of Default

Sector	Base Case	Best Case	Worst Case
Agriculture, Fishing & Forestry	21.00%	21.00%	21.00%
Mining and Quarrying	10.00%	10.00%	10.00%
Manufacturing	16.00%	16.00%	16.00%
Electricity & Water	10.00%	10.00%	11.00%
Building & Construction	25.00%	24.00%	25.00%
Wholesale & Retail Trade	15.00%	14.00%	15.00%
Transport & Communication	10.00%	10.00%	11.00%
Tourism, Restaurant & Hotels	7.00%	6.00%	7.00%
Real Estate	11.00%	11.00%	11.00%
Finance & Insurance	11.00%	11.00%	11.00%
Social Community & Personal Services	7.00%	7.00%	7.00%

Lifetime Probability of Default

Sector	Base Case	Best Case	Worst Case
Agriculture, Fishing & Forestry	58.00%	57.00%	59.00%
Mining and Quarrying	32.00%	31.00%	32.00%
Manufacturing	45.00%	44.00%	46.00%
Electricity & Water	31.00%	31.00%	32.00%
Building & Construction	63.00%	62.00%	64.00%
Wholesale & Retail Trade	39.00%	38.00%	40.00%
Transport & Communication	33.00%	32.00%	34.00%
Tourism, Restaurant & Hotels	34.00%	33.00%	35.00%
Real Estate	32.00%	32.00%	33.00%
Finance & Insurance	22.00%	21.00%	23.00%
Social Community & Personal Services	24.00%	23.00%	24.00%

Predicted relationships between the key indicators and sector wise default and loss rates of financial assets have been developed based on analysing historical data over the past 10 to 15 years.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Incorporation of forward-looking information (Continued)

Uncertain events

Uncertain events that are relevant to the risk of default occurring but for which, despite best efforts, the bank is not able to estimate the impact on ECL because of lack of reasonable and supportable information include:

1. Impact of the slowing down global economy on the growth rate of the Kenyan Economy
2. The unpredictable volatility of the global oil prices and its impact on the Kenyan Economy. This is specially the case when is Kenya is a net importer.
3. Unpredictable weather conditions considering Kenya is a predominately agricultural economy.
4. The unpredictable political environment both local and regional which has a direct impact on economic performance.
5. The rising impact of the Kenya's debt to GDP ratio and its impact on the economic output.
6. Impact of COVID-19 on the operations of business within the Kenyan Economy

Key Assumptions

In all the three scenarios of Base, Best and Worst case positive GDP growth is assumed. This assumption is well reasoned given the tested resilience strength of the Kenyan Economy during distress times.

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value in accordance with the accounting policy.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

When modification results in derecognition, a new loan is recognised and allocated to Stage 1 (assuming it is not credit-impaired at that time).

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Modified financial assets (Continued)

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities) to maximise collection opportunities and minimise the risk of default. Under the Bank's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. The Bank Credit Committee regularly reviews reports on forbearance activities.

For financial assets modified as part of the Bank's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Bank's ability to collect interest and principal and the Bank's previous experience of similar forbearance action. As part of this process, the Bank evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired. A customer needs to demonstrate consistently good payment behaviour over a period of time before the exposure is no longer considered to be credit-impaired/in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to Stage 1.

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- probability of default (PD);
- loss given default (LGD); and
- exposure at default (EAD).

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD.

The methodology of estimating PDs is discussed above under the heading 'Generating the term structure of PD'.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Measurement of ECL (Continued)

For loans secured by retail property, LTV ratios are a key parameter in determining LGD. LGD estimates are recalibrated for different economic scenarios and, for real estate lending, to reflect possible changes in property prices. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortisation. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EADs are potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts. For financial guarantees, the EAD represents the amount of the guaranteed exposure when the financial guarantee becomes payable. For some financial assets, EAD is determined by modeling the range of possible exposure outcomes at various points in time using scenario and statistical techniques.

As described above, and subject to using a maximum of a 12-month PD for Stage 1 financial assets, the Bank measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for credit risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

However, for overdrafts facilities that include both a loan and an undrawn commitment component, the Bank measures ECL over a period longer than the maximum contractual period if the Bank's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Bank's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are managed on a collective basis. The Bank can cancel them with immediate effect but this contractual right is not enforced in the normal day-to-day management, but only when the Bank becomes aware of an increase in credit risk at the facility level.

This longer period is estimated taking into account the credit risk management actions that the Bank expects to take, and that serve to mitigate ECL. These include a reduction in limits, cancellation of the facility and/or turning the outstanding balance into a loan with fixed repayment terms.

Where modeling of a parameter is carried out on a collective basis, the financial instruments are Banked on the basis of shared risk characteristics that include:
- instrument type;
- collateral type;
- remaining term to maturity;
- industry;

The groupings are subject to regular review to ensure that exposures within a particular Bank remain appropriately homogeneous.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Inputs, assumptions and techniques used for estimating impairment (Continued)

Measurement of ECL (Continued)

For portfolios in respect of which the Bank has limited historical data, external benchmark information is used to supplement the internally available data. The Bank does not have portfolios for which external benchmark information represents a significant input into measurement of ECL.

Loss allowance

The following tables show reconciliations from the opening to the closing balance of the loss allowance by class of financial instrument.

Loans and advances to customers	Stage 1 12-month ECL Shs	Stage 2 Lifetime ECL Shs	Stage 3 Lifetime ECL Shs	Total Shs
Loss allowance as at 1 January 2020	98,823	98,416	232,427	**429,666**
Changes in the loss allowance:	-	-	-	
– Transfer to stage 1	-	-	-	**-**
– Transfer to stage 2	(5,135)	5,135	-	**-**
– Transfer to stage 3	(869)	-	869	**-**
New financial assets originated	20,938	-	-	**20,938**
Financial assets derecognized	(14,020)	(14,898)	(57,309)	**(86,227)**
Financial Assets remeasured	60,326	(3,796)	60,159	**116,689**
Loss allowance as at 31 December 2020	**160,062**	**84,857**	**236,146**	**481,065**

More information about the significant changes in the gross carrying amount of financial assets during the period that contributed to changes in the loss allowance, is provided at the table below:

Loans and advances to customers	Stage 1 12-month ECL Shs	Stage 2 Lifetime ECL Shs	Stage 3 Lifetime ECL Shs	Total Shs
Gross carrying amount as at 31 December 2019 & 1 January 2020	5,206,471	903,227	782,931	6,892,629
Changes in the loss allowance:				
– Transfer to stage 1				**-**
– Transfer to stage 2	(270,528)	270,528		**-**
– Transfer to stage 3	(45,789)		45,789	**-**
New financial assets originated	1,103,097			**1,103,097**
Financial assets that have been derecognised	(738,651)	(136,726)	(57,309)	**(932,686)**
Financial Assets remeasured	245,433			**245,433**
Gross carrying amount as at 31 December 2020	**5,500,033**	**1,037,029**	**771,411**	**7,308,473**

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Loss allowance (Continued)

The following table provides a reconciliation between:

- amounts shown in the above tables reconciling opening and closing balances of loss allowance per class of financial instrument; and
- the 'impairment losses on financial instruments' line item in the consolidated statement of profit or loss and other comprehensive income.

In thousands Kenya Shillings	**Advances to customers at amortised cost**	**Cash and cash equivalents**	**Financial lease Receivable**	**Total**
Net re-measurement of loss allowance	108,165	-	-	108,165
Recoveries of amounts previously written off	-	-	-	-
Total	108,165	-		108,165

Credit-impaired financial assets

Credit-impaired loans and advances are graded 3 to 5 in the Bank's internal credit risk grading system (see Note 3(A (i))).

The following table sets out a reconciliation of changes in the net carrying amount of credit- impaired loans and advances to customers.

In thousands Kenya Shillings	2020	2019
Credit-impaired loans and advances to customersat 1 January	429,666	415,640
Change in allowance for impairment (Day 1 Adjustment)	-	-
Classified as credit-impaired during the year		-
Transferred to not credit-impaired during the year	108,165	14,026
Credit Impaired written off during the year	(56,766)	-
Credit-impaired loans and advances to customersat 31 December	481,065	429,666

The contractual amount outstanding on financial assets that were written off during the year ended 31 December 2020 and that are still subject to enforcement activity is Shs Nil (2019: Shs Nil million).

Modified financial assets

There were financial assets that were modified while they had a loss allowance measured at an amount equal to lifetime ECL.

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iii) Amounts arising from ECL (Continued)

Modified financial assets (Continued)

Loans with renegotiated terms

Loans with renegotiated terms are defined as loans that have been restructured due to deterioration in the borrower's financial position, for which the Bank has made concessions by agreeing to terms and conditions that are more favourable for the borrower than the Bank had provided initially and that it would not otherwise consider. A loan continues to be presented as part of loans with renegotiated terms until maturity, early repayment or write-off.

iv) Concentration of credit risk

The Bank monitors concentrations of credit risk by sector and by geographic location. An analysis of concentrations of credit risk from loans and advances, loan commitments, financial guarantees and investment securities is shown below.

(i) Advances to customers

	2020		2019	
	Sh '000	%	Sh '000	%
Agriculture, Fishing & Forestry	499,953	7	322,712	5
Mining and Quarrying	113,958	2	118,347	2
Manufacturing	333,391	5	372,979	5
Electricity & Water	206,285	3	55,855	1
Building & Construction	398,737	5	351,028	5
Wholesale & Retail Trade	2,680,167	37	2,741,552	40
Transport & Communication	450,572	6	304,295	4
Finance & Insurance	77,801	1	6,018	1
Real Estate	2,007,448	27	2,010,477	29
Tourism, Restaurant & Hotels	236,107	3	286,782	4
Social, Community & Personal Services	304,056	4	322,584	4
Total	7,308,475	100	6,892,629	100

(ii) Customer deposits

Private enterprises	6,399,716	69	6,579,206	76
Not for profit institutions and individuals	2,865,718	31	1,899,678	24
Total	9,265,434	100	8,478,884	100

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

iv) Concentration of credit risk (Continued)

(iii) Off – balance sheet items

Business services	43,582	7	46,305	7
Wholesale and retail	504,310	81	535,820	81
Transport and communications	24,904	4	26,460	4
Other	49,810	8	52,920	8
Total	622,606	100	661,505	100

v) Offsetting financial assets and financial liabilities

There were no financial assets and financial liabilities that were offset in the Bank's statement of financial position and none are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments.

Judgement	Retail & Corporate
Determination of whether the credit risk of financial instruments have increased significantly since initial recognition	Although COVID-19 has had a negative impact on the economic environment in the country, in isolation COVID-19 initially reflected a liquidity constraint due to the control measures imposed by the government more than an inherent increase in credit risk for the entire portfolio of advances held by the group. As such the bank did not impose a blanket downgrade on all ECL stages. A more targeted approach to the impact of COVID-19 on the bank's customer base was undertaken, following the bank's existing credit framework, which allowed for well-balanced and consistent decision-making that considered not only the impact of COVID-19, but existing economic trends, business sector, history of the client with the bank, value & type of security etc. As such, the bank did not view requests for payment deferrals as the sole indicator that SICR had occurred for performing advances. IFRS 9 contains a rebuttable presumption that credit risk has increased significantly when contractual payments are more than 30 days past due. This means that where payments are 30 days past due, the financial asset needs to migrate from stage 1 to stage 2. Instead of rebutting this presumption, the bank views that where the customer and the bank have agreed to a deferral of payment for a specified period, that such an extension will not trigger the counting of days past due.
SICR assessment of COVID 19 relief exposures	In accordance with IFRS 9, all exposures are assessed to determine whether there has been a SICR at each reporting date (monthly), in which case the expected credit loss is calculated on a lifetime basis. SICR triggers are based on client behaviour, sectorial performance (such as belonging to an industry in distress,are considered in the context of the financial impact of COVID-19), any significant change in the value of the underlying security and customer specific judgmental factors (e.g. duration in business or demise of a key man etc). Any adverse change in these triggers reflective of a significant increase in credit risk.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

<table>
<tr><th>Judgement</th><th>Retail & Corporate</th></tr>
<tr><td>Sensitivity Staging</td><td>
As outlined above, when there is a SICR since initial recognition, the exposure is moved from stage 1 to stage 2 and the ECL is calculated based on lifetime expected credit losses.
The move from 12-month expected credit loss to lifetime expected credit loss can result in a substantial increase in ECL. The sensitivity information provided in the table below details the additional ECL charge to the income statement that the bank would need to recognise if all facilities with greater than 90 days past due and all restructures were restaged.
<table>
<tr><th></th><th colspan="2">31 December 2020</th></tr>
<tr><td></td><td>Base</td><td>Restaged</td></tr>
<tr><td>Stage 1</td><td>4,650</td><td>14,064</td></tr>
<tr><td>Stage 2</td><td>-</td><td>-</td></tr>
<tr><td>Stage 3</td><td>-</td><td>-</td></tr>
<tr><td>Total</td><td>4,650</td><td>14,064</td></tr>
</table>
Comparative information has not been provided. As IFRS 9 is refined and embedded in the bank's reporting process, additional disclosure is included. This information was not produced in the prior year.
The following table sets out the additional ECL charge to the income statement if all advances which were subject to a form of COVID-19 relief were deemed to have suffered a SICR and were moved from stage 1 to stage 2, or where the COVID-19 relief was deemed to be an indicator of impairment and the advance was moved from stage 2 to stage 3 as at 31 December 2020.
<table>
<tr><th></th><th colspan="2">31 December 2020</th></tr>
<tr><td></td><td>Base</td><td>Restaged</td></tr>
<tr><td>Stage 1</td><td>4,650</td><td>14,064</td></tr>
<tr><td>Stage 2</td><td>9,957</td><td>27,276</td></tr>
<tr><td>Stage 3</td><td>-</td><td>-</td></tr>
<tr><td>Total</td><td>14,607</td><td>41,340</td></tr>
</table>
The increase in the loss allowance is calculated as the difference between the impairment that would have been raised in either stage 2 or stage 3 and the impairment recognised as at 31 December 2020. The impairment recognised as at 31 December 2020 already includes the post-model adjustment for COVID-19 relief detailed in the post-model adjustment section in this note.
</td></tr>
</table>

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

A CREDIT RISK (CONTINUED)

Judgement	Retail & Corporate
Treatment of financial relief offered in response to the impacts of COVID-19	The bank offered financial relief through various mechanisms in response to COVID- 19. These included the following: • additional facilities or new loans being granted; • reschedule of existing exposures with no change in the present value of the estimated future cash flows; and • reschedule of existing exposures with the view of offering between 6 to 12months of repayment of principal relief. • Waiver of fees such as commitment fees etc. • Reduction/ partial waiver in interest rates charged. Prior to COVID-19 relief being granted, the customer was assessed against eligibility for relief criteria. In doing so, the bank was able to identify customers who were in good standing but were facing financial distress due to the impact of COVID-19 directly or indirectly. The COVID-19 relief provided to these customers was deemed to be temporary and cash flow in nature. Where a customer was already experiencing financial distress and was in arrears prior to 31 March 2020, any restructuring of the customer's facilities was deemed to be permanent in nature. Where relief is expected to be temporary in nature and as such qualifies as a non- distressed restructure, the staging of the exposure as at 31 March 2020 has been maintained, and adjustments have been made to coverage to allow for incremental credit risk and potential masking of normal arrears. Where the relief is expected to be permanent in nature, the exposure has been treated as a distressed restructure, and staging and coverage have been adjusted in line with the bank's normal practice. Where relief has been enacted through the issuance of a new loan as part of a non-distressed restructure, the loan has been treated at initial recognition as a new exposure and coverage has been calculated on the basis of sectorial probability of default, including a post-model adjustment to allow for incremental credit risk attributable to COVID-19 relief provided. Where the relief provided as an emergency facility (as defined under CBK's issued guidelines to the banks on implementation of emergency measures to mitigate the adverse impact of COVID-19 pandemic on loans and advances (Circulars No 3 and 4).) is part of a distressed restructure, the staging of the emergency facility has been aligned to the staging of the underlying exposures. Where there are multiple underlying exposures with different stages, the worst of these stages has been applied. The ECL for all exposures on which relief has been offered and for all emergency facilities has been adjusted to reflect the impact of forward-looking macroeconomic information in line with the rest of the portfolio.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

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, 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.

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 2020 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 key measure used by the company for managing liquidity risk is the ratio of net liquid assets to deposits from customers. The table below details the liquidity ratio trends over the year:

As at 31 December	2020	2019
	%	%
Average for the period	43	44
Maximum for the period	45	48
Minimum for the period	39	41
Statutory minimum requirement by Central Bank	20	20
	====	====

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 discounted 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

B LIQUIDITY RISK

Undiscounted cash flows (Continued)

	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 2020						
FINANCIAL ASSETS						
Cash and balances with CBK	351,201	325,918	37,277	38,774	-	753,170
Deposits and balances from banking institutions	528,121					528,121
Government securities	737,427	296,447	904,344	253,097	637,716	2,829,031
Advances to customers	553,077	1,134,371	1,503,862	2,883,810	752,288	6,827,408
	2,169,826	1,756,736	2,445,483	3,175,681	1,390,004	10,937,730
FINANCIAL LIABILITIES						
Customer deposits	1,608,887	6,207,968	710,028	738,551	-	9,265,434
	1,608,887	6,207,968	710,028	738,551	-	9,265,434
Net liquidity gap	560,939	(4,451,232)	1,735,455	2,437,130	1,390,004	1,672,296
As at 31 December 2019						
Total financial assets	1,486,927	1,795,110	2,651,257	3,051,627	1,030,090	10,015,012
Total financial liabilities	1,448,123	6,175,334	657,070	198,358	-	8,478,885
Net liquidity gap	38,804	(4,380,224)	1,994,187	2,853,269	1,030,090	1,536,127

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

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (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 (Continued)

C MARKET RISK

(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						119,126	119,126
Balances with Central Bank of Kenya						634,044	634,044
Deposits and balances due from banking institutions						528,121	528,121
Government securities	737,427	296,447	904,344	253,097	637,716		2,829,031
Advances to customers	553,077	1,134,371	1,503,862	2,883,810	752,288		6,827,408
Total financial assets	1,290,504	1,430,818	2,408,206	3,136,907	1,390,004	1,281,291	10,937,730
FINANCIAL LIABILITIES							
Customer deposits	410,161	6,207,968	710,028	738,551	-	1,198,726	9,265,434
Total financial liabilities	410,161	6,207,968	710,028	738,551	-	1,198,726	9,265,434
Interest rate sensitivity gap	880,343	(4,777,150)	1,698,178	2,398,356	1,390,004	82,565	1,672,296
As at 31 December 2019							
Total financial assets	433,658	6,839,627	1,166,101	259,426	429,041	887,159	10,015,012
Total financial liabilities	362,845	6,175,334	657,070	198,358	-	1,085,278	8,478,885
Interest rate sensitivity gap	70,813	664,293	509,031	61,068	429,041	(198,119)	1,536,127

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 (Continued)

C MARKET RISK

(i) Interest rate risk (Continued)

Exposure to interest rate risk

The group 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 2020

	Amount Sh'000	Scenario 10% Increase in net margin Sh'000	Scenario 10% Decrease in net margin Sh'000
Profit before taxation	96,554	139,150	53,957
Adjusted core capital	1,746,944	1,789,541	1,704,347
Adjusted total capital	1,746,944	1,789,541	1,704,347
Risk weighted assets (RWA)	7,064,332	7,064,332	7,064,332
Adjusted core capital to RWA	25%	25%	24%
Adjusted total capital to RWA	25%	25%	24%
	=======	=======	========

Interest rate risk – stress test-as at 31 December 2019

	Amount Sh'000	Scenario 10% Increase in net margin Sh'000	Scenario 10% Decrease in net margin Sh'000
Profit before taxation	85,643	133,256	48,206
Adjusted core capital	1,660,600	1,703,125	1,618,075
Adjusted total capital	1,660,600	1,703,125	1,618,075
Risk weighted assets (RWA)	6,790,811	6,790,811	6,790,811
Adjusted core capital to RWA	24%	26%	24%
Adjusted total capital to RWA	24%	26%	24%
	=======	=======	=======

ii) Foreign exchange risk

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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

C MARKET RISK (CONTINUED)

ii) Foreign exchange risk (Continued)

Management of foreign exchange risk (Continued)

The bank's currency position is as follows:

	SHS Sh '000	GBP Sh '000	USD Sh '000	EURO Sh '000	OTHERS Sh '000	Total Sh '000
At 31 December 2020						
FINANCIAL ASSETS						
Cash in hand	77,922	2,128	22,623	16,252	200	119,126
Balances with CBK	623,119	618	84,480	3,094	374	711,685
Deposits and balance due from banking institutions	6,989	329,485	101,554	8,334	4,119	450,480
Government securities	2,829,031					2,829,031
Other securities						
Advances to customers	6,151,813	989	615,035	59,572	-	6,827,408
Other assets	130,856	-	-			130,856
Total financial assets	9,819,729	333,220	823,692	87,251	4,693	11,068,585
FINANCIAL LIABILITIES						
Customer deposits	8,115,209	330,945	736,454	82,827	-	9,265,434
Other liabilities	102,205	-	-	-	-	102,205
Total financial liabilities	8,217,414	330,945	736,454	82,827	-	9,367,639
Net balance sheet position	1,602,315	2,275	87,238	4,425	4,693	1,700,946
At 31 December 2019						
Total financial assets	9,106,710	259,196	647,135	110,547	8,654	10,132,242
Total financial liabilities	7,498,259	261,591	678,213	108,322	-	8,546,385
Net balance sheet position	1,608,451	(2,395)	(31,078)	2,225	8,654	1,585,857

3 FINANCIAL RISK MANAGEMENT (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.

	Amount Sh'000	Scenario 10% Increase in foreign currency rate Sh'000	Scenario 10% Decrease in foreign currency rate Sh'000
At 31 December 2020			
Profit before taxation	96,554	105,948	87,160
Adjusted core capital	1,746,944	1,766,338	1,747,550
Adjusted total capital	1,746,944	1,766,338	1,747,550
Risk weighted assets (RWA)	7,064,332	7,064,332	7,064,332
Adjusted core capital to RWA	25%	25%	25%
Adjusted total capital to RWA	25%	25%	25%
	=======	=======	========
At 31 December 2019			
Profit before taxation	85,643	82,729	88,978
Adjusted core capital	1,660,600	1,657,475	1,663,725
Adjusted total capital	1,660,600	1,657,475	1,663,725
Risk weighted assets (RWA)	6,790,811	6,790,811	6,790,811
Adjusted core capital to RWA	24%	24%	24%
Adjusted total capital to RWA	24%	24%	24%
	=======	=======	=======

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 no impact on shareholders' equity (2019: Nil).

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.

3 FINANCIAL RISK MANAGEMENT (Continued)

D CAPITAL MANAGEMENT

Regulatory capital (Continued)

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 2019, 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 2019.

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.

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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

D CAPITAL MANAGEMENT

Regulatory capital (Continued)

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

	Nominal financial position amounts		Risk weighted amounts	
	2020	2019	2020	2019
ASSETS	Sh'000	Sh'000	Sh'000	Sh'000
Cash (including foreign notes and coins)	119,126	124,949	-	-
Cash balances with Central Bank of Kenya	634,044	762,210	-	-
Government securities	2,829,031	2,231,232	-	-
Corporate bonds	-	-	-	-
Deposits and balances due from banking Institutions	528,121	433,658	90,094	76,739
Loans and advances to customers	6,827,408	6,462,963	5,040,046	4,631,391
Other assets	130,856	127,365	130,856	127,365
Investment in subsidiary	10,000	1,000	10,000	1,000
Property and equipment	33,823	45,261	33,823	45,261
Intangible assets	5,842	7,324	5,842	7,324
Deferred tax asset	154,354	117,827	154,354	117,827
Right of Use Asset	88,308	112,088	88,309	112,088
Tax recoverable	17,418	17,418	17,418	17,418
Total assets on balance sheet	11,378,331	10,443,295	5,570,742	5,136,413
Total asset off balance sheet	622,606	661,506	264,202	238,165
Total allowance for operations risk			941,944	868,031
Total allowance for market risk			297,444	549,202
Total risk weighted assets	12,000,937	11,104,801	7,074,332	6,791,811
Tier 1 Capital	1,746,944	1,660,600		
Tier 1 + Tier 2 Capital	1,746,944	1,660,600		
Basel ratio				
Tier 1 (CBK minimum – 10.5%)	25%	24%		
Tier 1 + Tier 2 (CBK min – 14.5%)	25%	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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (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 - 2020. 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.

3 FINANCIAL RISK MANAGEMENT (Continued)

E OPERATING RISK

ii) Bank operational risk (Continued)

Management of operational risk (Continued)

An examples of a KPI is 'Incident/Fraud/ Suspicious Activities and Transaction Reports. ' 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 has 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (Continued)

E OPERATING RISK

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

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.

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 Wolfsburg-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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3 FINANCIAL RISK MANAGEMENT (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).

4 INTEREST INCOME

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
Advances to customers	887,929	808,545	887,929	808,545
Government securities – at amortised cost	138,173	186,786	138,173	186,786
Government Securities – at fair value	84,312	37,324	84,312	37,324
Corporate bonds - at amortised cost	-	2,527	-	2,527
Deposits/balances due from other financial institutions	3,338	4,483	3,338	4,483
	1,113,752	1,039,665	1,113,752	1,039,665

5 INTEREST EXPENSE

Customer deposits	672,799	633,320	672,799	633,320

6 FEES AND COMMISSION INCOME

Transaction related fees	61,979	39,286	58,030	35,497
Credit related fees and commissions	17,511	27,398	17,511	27,398
	79,490	66,684	75,541	62,895

7 GAINS 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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

		GROUP		BANK	
		2020	2019	2020	2019
		Sh'000	Sh'000	Sh'000	Sh'000
8	OTHER OPERATING (LOSS)/INCOME				
	Locker rental income	940	1,136	940	1,136
	Other operating income	18,081	6,350	18,081	6,350
	Fair value gain/(loss) on financial assets (note 15)	15,405	(19,461)	15,405	(19,461)
		34,426	(11,975)	34,426	(11,975)
		======	======	======	======

		GROUP		BANK	
		2020	2019	2020	2019
		Sh'000	Sh'000	Sh'000	Sh'000
9	OPERATING EXPENSES				
	Staff costs (note 10)	129,837	140,810	128,014	139,103
	Contribution to Deposit Protection Fund	12,675	12,112	12,675	12,112
	Depreciation on equipment (note 20)	15,923	19,118	15,923	19,118
	Amortisation of intangible assets (note 21)	3,071	3,531	3,006	3,501
	Directors' emoluments	26,456	31,096	26,456	31,096
	Auditors' remuneration	11,697	11,146	11,347	10,795
	Rent and rates	9,318	8,927	9,318	8,927
	Legal and professional fees	16,349	14,559	16,349	14,559
	Insurance	7,416	7,500	7,416	7,501
	Security	13,452	13,589	13,452	13,589
	Telephone and postage	10,562	11,101	10,562	11,101
	Repairs and maintenance	16,450	6,515	16,450	6,515
	Other expenses	47,500	57,641	46,298	56,871
	Depreciation on Right of Use Asset (note 16)	23,780	23,780	23,780	23,780
	Finance cost on lease liabilities (note 26)	8,250	9,664	8,250	9,664
		352,736	371,089	349,296	368,231
		======	======	======	======
10	STAFF COSTS				
	Salaries and allowances	123,271	131,957	121,448	130,316
	Staff training	635	2,014	635	2,014
	Terminal dues	598	983	598	983
	Pension contributions-defined contribution scheme	4,497	5,043	4,497	4,977
	Medical expenses	836	813	836	813
		129,837	140,810	128,014	139,103
		======	======	======	======

	GROUP 2020	GROUP 2019	BANK 2020	BANK 2019
	Sh'000	Sh'000	Sh'000	Sh'000
11 TAXATION				
(a) Taxation credit				
Current taxation based on the taxable profit for the period at 25%	121	281	-	-
Deferred taxation (credit) (note 22):-				
- current year (credit)	2,762	(5,309)	2,743	(5,306)
- prior year (under)/ over provision	(39,270)	(1)	(39,270)	-
	(36,387)	(5,029)	(36,527)	(5,306)
(b) Reconciliation of taxation credit to the expected taxation based on profit before taxation				
Profit before taxation	97,063	86,574	96,554	85,643
Tax at the applicable rate of 30%	29,093	25,972	28,966	25,693
Effect of expenses disallowed for taxation purposes	5,212	6,053	5,199	6,054
Effect of income not subject to taxation	(31,422)	(37,053)	(31,422)	(37,053)
Prior year (under)/ over provision	(39,270)	(1)	(39,270)	-
Taxation credit	(36,387)	(5,029)	(36,527)	(5,306)
(c) Corporate tax recoverable				
At 1 January	17,455	17,479	17,418	17,418
Taxation charge	(121)	(281)	-	-
Tax paid in the year	299	257	-	-
At 31 December	17,633	17,455	17,418	17,418

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 2020	GROUP 2019	BANK 2020	BANK 2019
Earnings				
Earnings for the year attributable to ordinary shareholders (Sh'000)	133,450	91,603	133,081	90,949
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	133.45	91.60	133.08	90.95

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 2020 or 31 December 2019, respectively.

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
13 CASH AND BALANCES WITH CENTRAL BANK OF KENYA				
Cash on hand	119,126	124,949	119,126	124,949
Balances with Central Bank of Kenya				
- Deposits held under lien	10,925	10,135	10,925	10,135
- Current account with CBK	623,119	752,075	623,119	752,075
	753,170	887,159	753,170	887,159
	753,170	887,159	753,170	887,159

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 2020 the cash reserve ratio requirement was 5.25% (2019: 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.

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
14 DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS				
Balances due from banking institutions	528,121	433,658	528,121	433,658

The weighted average effective interest rate for deposits and balances due from banking institutions at 31 December 2020 was 6.0% (2019 – 8.5%).

	GROUP & BANK	
	2020	2019
MATURITY ANALYSIS OF DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS	Sh'000	Sh'000
Due on demand	528,121	433,658

	GROUP & BANK	
	2020	2019
	Sh'000	Sh'000
15 GOVERNMENT SECURITIES		
Treasury bills – at amortised cost		
At amortized cost – maturing within 90 days		
Face value	1,800,000	1,250,000
Less: unearned discount	(37,751)	(47,203)
	1,762,249	1,202,797
At amortised cost (maturing within 5 years)		-
At amortised cost (maturing after 5 years)	273,309	-
Treasury bonds at fair value	793,473	1,028,435
	1,066,782	1,028,435
	2,829,031	2,231,232

The weighted average effective interest rate for treasury bonds as at 31 December 2020 was 8.64% (2019 – 9.43%).

Included in Government Bonds maturing within 5 years is an impairment provision of Sh 9,277,557 (2019: 9,277,557).

Movement in treasury bonds can be summarised as follows:

	GROUP & BANK	
	2020	2019
	Shs'000	Shs'000
At 1 January	1,028,435	-
Additions	250,000	2,871,457
Disposals	(227,058)	(1,823,561)
Net (loss)/gain	15,405	(19,461)
At 31 December	1,066,782	1,028,435

The weighted average effective interest rate on the bonds at 31 December 2020 was 8.1% (2019 – 7%).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 RIGHT-OF-USE ASSETS – GROUP & BANK

The Group leases office space and equipment for its use. Information about the leases in which the Group is a lessee is presented below:

	2020 Sh'000	2019 Sh'000
COST		
At 1 January as previously reported	135,868	-
Adjustment on adoption of IFRS 16	-	135,868
At 31 December	135,868	135,868
DEPRECIATION		
At 1 January	23,780	-
Charge for the year	23,780	23,780
At 31 December	47,560	23,780
NET BOOK VALUE		
At 31 December	88,308	112,088

Amounts recognised in profit and loss

Depreciation expense on right-of-use	23,780
Interest expense on lease liabilities	8,250
At the end of the year	32,030

The Group is not committed to any arrangements that are short term as at year-end.

All of the property and equipment leases in which the Group is the lessee contain only fixed payments.

The total cash outflow for leases amount to Sh 27.5 million (2019: Sh 26.8 million).

There are no restrictions or covenants imposed by lessors and the Group did not enter into any sale and leaseback transactions during the year (2019: Nil)

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
17 ADVANCES TO CUSTOMERS				
Loans and advances to customers	7,307,573	6,891,729	7,307,573	6,891,729
Bills discounted	900	900	900	900
	7,308,473	6,892,629	7,308,473	6,892,629
Provision for impaired loans and advances (note 18)	(481,065)	(429,666)	(481,065)	(429,666)
	6,827,408	6,462,963	6,827,408	6,462,963

The weighted average effective interest rate on advances to customers as at 31 December 2020 was 13.24% (2019 – 12.82%).

Included in net advances are loans and advances amounting to Sh 545,265,000 (2019 – Sh 550,504,000), net of specific provisions, which have been classified as non-performing.

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
Analysis of gross advances by maturity:				
Maturing within one year	3,191,310	3,080,126	3,191,310	3,080,126
Over one year to three years	1,462,637	1,843,036	1,462,637	1,843,036
Over three to five years	2,654,526	1,969,467	2,654,526	1,969,467
	7,308,473	6,892,629	7,308,473	6,892,629

Advances to related parties are disclosed in note 31.

18 PROVISION FOR IMPAIRMENT LOSSES	GROUP		BANK	
	2020	2019	2020	2019
a) Impairment losses on loans and advances				
	Sh'000	Sh'000	Sh'000	Sh'000
At 1 January	429,666	415,640	429,666	415,640
Impairment losses/(reversals) in the year	108,165	14,026	108,165	14,026
Write Off	(56,766)	-	(56,766)	
At 31 December	481,065	429,666	481,065	429,666

NOTES TO THE FINANCIAL STATEMENTS (Continued)

18	PROVISION FOR IMPAIRMENT LOSSES	GROUP		BANK	
		2020	2019	2020	2019
	b) Total impairment losses/(reversals) on financial assets at amortised costs				
	Impairment losses/(reversals) on loans and advances in the year (Note 17)	108,165	14,026	108,165	14,026
	Impairment losses on government securities (Note 15)	-	(1,705)	-	(1,705)
		108,165	12,321	108,165	12,321
		=======	=======	=======	=======

19	OTHER ASSETS				
	Items in course of collection	9,053	9,602	9,053	9,602
	Prepayments	57,054	49,708	57,054	49,708
	Other receivables	72,482	67,783	64,749	68,055
		138,589	127,093	130,856	127,365
		=======	=======	=======	=======

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 2019	94,468	27,740	169,833	292,041
Additions	3,033	100	2,577	5,710
Disposals	-	(104)	-	(104)
At 31 December 2019	97,501	27,736	172,410	297,647
At 1 January 2020	97,501	27,736	172,410	297,647
Additions	4,339		317	4,656
Disposals	-	(2,560)	-	(2,560)
At 31 December 2020	101,840	25,176	172,727	299,743
DEPRECIATION				
At 1 January 2019	80,836	13,071	139,465	233,372
Charge for the year	5,796	5,291	8,031	19,118
Disposal	-	(104)	-	(104)
At 31 December 2019	86,632	18,258	147,496	252,386
At 1 January 2020	86,632	18,258	147,496	252,386
Charge for the year	3,884	4,732	7,307	15,923
Disposal	-	(2,387)	-	(2,387)
At 31 December 2020	90,516	20,603	154,803	265,920
NET BOOK VALUE				
At 31 December 2020	11,324	4,573	17,924	33,823
At 31 December 2019	10,869	9,478	24,914	45,261

Included in equipment are assets with a cost of Sh 57,491,093 (2019 - Sh 114,783,246), which were fully depreciated. The notional depreciation charge in respect of these assets for the year is Sh 8,623,664 (2019 – Sh 17,217,487).

	GROUP 2020 Sh'000	GROUP 2019 Sh'000	BANK 2020 Sh'000	BANK 2019 Sh'000
21 INTANGIBLE ASSETS - COMPUTER SOFTWARE				
COST				
At 1 January	47,328	47,271	47,052	47,052
Additions	1,524	57	1,524	-
At 31 December	48,852	47,328	48,576	47,052
AMORTISATION				
At 1 January	39,878	36,347	39,728	36,227
Charge for the year	3,071	3,531	3,006	3,501
At 31 December	42,949	39,878	42,734	39,728
NET BOOK VALUE				
At 31 December	5,903	7,450	5,842	7,324
	======	======	======	======

22 DEFERRED TAXATION

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

	GROUP 2020 Sh'000	GROUP 2019 Sh'000	BANK 2020 Sh'000	BANK 2019 Sh'000
Excess depreciation over capital allowances	6,066	5,646	6,067	5,658
Leave pay provision	393	1,285	393	1,285
Other provisions	4,773	4,773	4,773	4,773
Provisions for impairment	147,103	91,951	147,103	91,951
Unrealised exchange losses	(4,663)	18	(4,651)	-
Tax losses	669	14,160	669	14,160
	154,341	117,833	154,354	117,827
	======	=======	=======	=======

The movement on the deferred tax asset account is as follows:

	GROUP 2020 Sh'000	GROUP 2019 Sh'000	BANK 2020 Sh'000	BANK 2019 Sh'000
As at 1 January	117,833	112,523	117,827	112,521
Credit for the year – note 11(a)	(2,762)	5,309	(2,743)	5,306
Prior year under provision - note 11(a)	39,270	1	39,270	-
At 31 December	154,341	117,833	154,354	117,827
	======	=======	=======	=======

NOTES TO THE FINANCIAL STATEMENTS (Continued)

23 INVESTMENT IN SUBSIDIARY

			BANK	
			2020	2019
	No. of shares	Holding	Sh'000	Sh'000
Parabank Insurance Agency Limited	5,000	100%	10,000	1,000
	======	=====	======	======

The subsidiary is wholly owned Limited Liability Company incorporated and domiciled in Kenya. The company was incorporated on 22 May 2019 and licenced to operate Insurance Agency/brokerage business.

The principal activity of the company is insurance agency business.

24 CUSTOMER DEPOSITS

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
Current accounts	665,740	585,894	673,210	585,894
Savings accounts	353,239	324,337	353,239	324,337
Call deposits	488,726	460,239	488,726	460,239
Fixed deposits	7,750,259	7,102,365	7,750,259	7,108,414
	9,257,964	8,472,835	9,265,434	8,478,884
	========	========	========	========
Analysis of customer deposits by maturity:				
Payable within 90 days	7,809,395	6,960,339	7,816,855	6,966,388
Payable after 90 days and within one year	710,028	657,070	710,028	657,070
Payable after one year	738,551	855,426	738,551	855,426
	9,257,964	8,472,835	9,265,434	8,478,884
	========	========	========	========

The weighted average effective interest rate on interest bearing customer deposits at 31 December 2020 was 7.6 % (2019 – 8.33%).

Customer's deposits from related parties are disclosed in note 31 and concentrations of customer deposits are covered under note 3(a).

25 OTHER LIABILITIES

	GROUP		BANK	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
Sundry payables	85,305	52,203	81,440	48,489
Accruals	19,453	14,726	19,453	14,726
Premiums payable	-	-	-	-
Leave pay provision	1,312	4,285	1,312	4,285
	106,070	71,214	102,205	67,500
	======	======	======	======

NOTES TO THE FINANCIAL STATEMENTS (Continued)

26 LEASE LIABILITIES

	GROUP & BANK	
	2020	2019
	Sh'000	Sh'000
Undiscounted future minimum lease payment under operating lease at 1 January	64,775	64,775
Impact of discounting	(37,402)	(37,402)
Leases not yet commenced at 1 January	108,495	108,495
At 1 January	135,868	135,868

The movement in the lease liabilities is as follows:

Balance at 1 January	118,694	135,868
Payment of lease liabilities	(27,550)	(26,838)
Interest on lease liabilities	8,250	9,664
At 31 December	99,394	118,694
Amounts due for settlement within 12 months	19,300	19,138
Amounts due for settlement after 12 months	80,094	99,556
	99,394	118,694

Maturity Analysis of undiscounted cash flows

Year 1	27,549	65,802
Year 2	28,737	52,002
Year 3	29,976	38,023
Year 4	23,003	6,356
Year 5	11,550	6,237
	120,815	168,420

The Company does not face a significant liquidity risk with regards to its lease liabilities. Lease liabilities are monitored within the company's treasury function. All lease obligations are denominated in Kenya Shillings.

	GROUP & BANK	
	2020	2019
	Sh'000	Sh'000

27 SHARE CAPITAL

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 generated from operations

	GROUP		BANK	
	2020	2019	2020	2019
	Sh '000	Sh '000	Sh '000	Sh '000
Profit before taxation	97,063	86,574	96,554	85,643
Adjustments for:				
Depreciation on equipment (note 20)	15,923	19,118	15,923	19,118
Depreciation on right of use asset (note 16)	23,780	23,780	23,780	23,780
Amortization of intangible assets (note 21)	3,071	3,531	3,006	3,501
Gain on sale of motor vehicle	(329)	(15)	(329)	(15)
Interest on lease liabilities (note 26)	8,250	9,664	8,250	9,664
Working capital changes :	147,788	142,652	147,184	141,691
Increase in balances held by Central Bank of Kenya under lien	(790)	50	(790)	50
Increase in advances to customers	(364,445)	(820,334)	(364,445)	(820,334)
(Increase)/decrease in government securities	(597,799)	340,149	(597,799)	340,149
Decrease in corporate bonds	-	35,695	-	35,695
Increase in other assets	(11,496)	(17,901)	(3,491)	(18,177)
Increase in customer deposits	785,129	351,401	786,550	352,701
Increase/(decrease) in other liabilities	34,856	(6,082)	34,705	(6,459)
Cash generated from operations	(6,787)	25,630	1,914	25,316

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

Cash on hand (note 13)	119,126	124,949	119,126	124,949
Deposits and balances due from banking institutions	528,121	433,658	528,121	433,658
Current account with Central Bank of Kenya	623,119	752,075	623,119	752,075
	1,270,366	1,310,682	1,270,366	1,310,682

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

	2020	2019
	Sh'000	Sh'000
(a) Contingent liabilities		
Letters of credit	-	48,685
Letters of guarantee and performance bonds	563,468	523,557
Bills for collection	59,138	89,264
	622,606	661,506

Letters of credit are commitments by the bank to make payments to third parties, on production of documents, on behalf of customers and are reimbursable 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 2020 amounted to Sh 7,250,000 (2019- Sh 7,250,000).

(b) The Group had no capital commitments as at 31 December 2020 (2019 – 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.

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 2020 include placements made in the bank by directors, their associates and companies associated to directors. Advances to customers and deposits at 31 December 2020 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 2020 include guarantees and letters of credit for companies associated to directors.

30 RELATED PARTY TRANSACTIONS (Continued)

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

	Directors' associated companies		Employees/staff	
	2020	2019	2020	2019
	Sh'000	Sh'000	Sh'000	Sh'000
Movement in related party balances was as follows:				
Loans and advances:				
At 1 January	659,234	584,313	59,844	67,924
Net movement during the year	(16,923)	74,921	(8,858)	(8,080)
At 31 December	642,311	659,234	50,986	59,844
Interest earned	83,500	85,700	4,844	5,685
Deposits:				
At 1 January	438,188	476,975	8,672	12,373
Net movement during the year	(120,447)	(38,787)	(3,154)	(3,701)
At 31 December	317,741	438,188	5,518	8,672
Interest paid	28,597	43,819	441	780

	GROUP & BANK	
	2020	2019
	Sh'000	Sh'000
Guarantees and letters of credit to companies associated to directors	26,860	25,316

Key management compensation

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

	2020	2019
	Sh'000	Sh'000
Key management salaries and other benefits	65,379	66,472
Directors emoluments	26,456	31,093

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.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 FIDUCIARY ACTIVITIES

At 31 December 2020, the bank did not hold any asset security documents on behalf of customers (2019: none).

32 COUNTRY OF INCORPORATION

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

33 CURRENCY

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

34 EVENTS AFTER REPORTING PERIOD

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