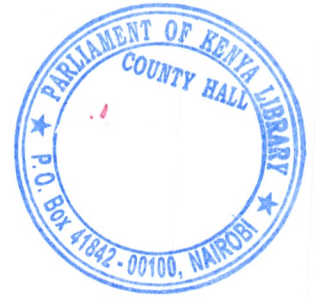
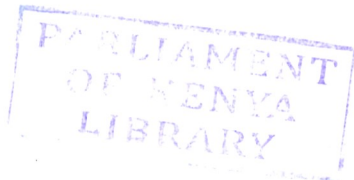


KENYA POST OFFICE SAVINGS BANK



My Bank, My Choice, My Future

**ANNUAL REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED**

31ST DECEMBER 2017

ANNUAL REPORT AND FINANCIAL STATEMENTS 31ST DECEMBER 2017

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BOARD OF DIRECTORS

The Kenya Post Office Savings Bank consists of a team of experienced and qualified professionals who provide leadership in matters relating to decision making in the Bank. The Board is appointed by the Minister of Finance and is made up of the Chairman, four Directors and the Managing Director. The Board provides guidance and direction to the Management. Directors are given appropriate and timely information so that they can maintain full and effective control over strategic, financial, operational and compliance requirements. The day-to-day running of Postbank has been delegated to the Managing Director. The Board retains responsibility for establishing and maintaining the internal controls over the strategic, financial, operational and compliance issues. The Board is responsible for ensuring succession, planning and recruitment of the CEO. The current Board is made up of the following;



Hon. Fred Kapondi

Hon. Fred Kapondi Chesebe holds a Bachelor of Arts degree (Hons) from the University of Nairobi. Prior to his appointment as Postbank Chairman, he served as the Member of Parliament for Mt. Elgon Constituency between 2008 and 2012. He has vast experience serving in various Parliamentary Committees and was the Chairman of the Parliamentary Committee on Administration and National Security between 2008 and 2012. Hon. Kapondi also served as a Member of the Parliamentary Committee on Budget 2008-2012; Member of Parliamentary Committee on Equal Opportunities 2010-2012; Member of Parliamentary House Privileges Committee and also Member, Liaison Committee. Hon. Kapondi is trained in Corporate Governance and has attended many local & International conferences. He was appointed as Chairman of Kenya Post Office Savings Bank on **10th January 2014**. Hon. Kapondi retired as the Chairman of Postbank on 31st January 2017.



Mr. Henry K Rotich, Cabinet Secretary, The National Treasury, EGH.

Mr. Henry K. Rotich is the Cabinet Secretary for National Treasury. Prior to his appointment, he was the Head of Macroeconomics at the Treasury, Ministry of Finance for 7 years. Prior to joining the Ministry of Finance, Mr. Rotich worked at the Central Bank of Kenya for 12 years. He was attached to the International Monetary Fund (IMF) local office in Nairobi as an economist between 2001-2004. He has been a Director of several Boards of State Corporations including; Insurance Regulatory Board, Industrial Development Bank, Communication Commission of Kenya and Kenya National Bureau of Statistics. Mr. Rotich holds a Master's Degree in Public Administration (MPA) from the Harvard Kennedy

School, Harvard University. He also holds MA and BA degrees in Economics (University of Nairobi).

Board of Directors (continued)



Mr. Nzomo Mutuku Alternate to Cabinet Secretary, The National Treasury

Mr. Nzomo Mutuku is since June 2013 the Senior Advisor, Financial Sector, at The National Treasury of Kenya where he advises on policy matters relating to Pensions, Insurance, Capital Markets, Banking and other financial services. Previously, he was the Chief Manager Research & Development at the Retirement Benefits Authority in Kenya. He worked at the Authority for over 12 years having previously worked in the Research Department of the Central Bank of Kenya. Mr. Mutuku holds a Masters of Arts degree in Economics as well as a first class honours Bachelor of Arts (Economics) degree from the University of Nairobi. He has also undertaken training in pensions and financial markets in various countries including the UK and Canada and at the Harvard University and Wharton Business School in the United States. He has authored a number of papers on financial sector issues including "The Case for Consolidated Financial Sector Supervision in Kenya and the impact of the Global Financial Crisis on the Pensions Sector in Kenya" which are widely quoted in the region. He was a member of the High Level Task Force that negotiated the East Africa Community Monetary Union Protocol. Mr. Nzomo retired as a board member of the Bank on 30th May 2017.



Ms. Jane Moronge Marwa

Ms. Jane Moronge Marwa holds a Post Graduate Masters of Education specializing in education and a Bachelor's Degree in Education both from the University of Nairobi. She has been a teacher for over 20 years serving in different schools before becoming a Director of Kuria Women of Valor Organization where she spearheads the recruitment and orientation of new members as well as assist in management of resources. She is the founder and Director of Elite Junior Academy in Isebania – Kuria. Ms. Moronge has been instrumental in the formation and development of Radio Lessons in Kenya Institute of Education and has empowered the Girl Child and vulnerable children in Kuria District. Ms. Moronge was an MP

candidate for 2013 general elections. She is currently studying for PhD in Education Foundation at the University of Nairobi. Jane retired as board member of Postbank in May 2017.

Board of Directors (continued)



Dr. Urbanus Kioko

Dr. Kioko holds a Doctorate Degree in Economics of the University of Nairobi (2008), Mphil (Health Economics) of the University of Cape Town (2000), MA (Econ) of the University of Nairobi (1994) and Bed (Business and Economics) of the University of Nairobi (1992). He is currently a steering committee member of the out-put-based approach (OBA) programme in the Ministry of Health, a coordinator for the MSc in Health Economics and Policy, member of the College Health and Safety Committee, Chair, Health Economics committee, School of Economics, University of Nairobi.



Mr. Lawrence Tanui

Mr. Lawrence Tanui has over 15 years' experience in business, insurance and accountancy. He is currently studying PhD in Business Management at Moi University, Mr. Tanui Holds an MBA in Strategic Management (UON), Bcom (Accounting) and he is a Certified Public Accountant (CPAK). He has developed his career in Finance and Accounts and is currently the Finance Manager at Africa Merchant Assurance Company Ltd (AMACO LTD).



Ms. Anne Waiyego Karanja

Anne has a Masters degree in Business Administration specializing in Strategic Management and a

Bachelor's degree in Economics and Sociology. She has vast experience in banking, auditing and finance. Prior to joining Kenya Post Office Savings Bank, Anne was an Auditor with the Controller and Auditor General. She has previously headed several departments in the bank including Finance & Accounts, Administration and Money Transfer Services. Anne has proven leadership, project and business management skills and has a passion for service excellence. She has also steered several business projects with remarkable success.

Board of Directors (continued)



Head of Legal, Security & Investigations/Company Secretary-

Mr Hannington Ouko

Mr. Hannington O. Ouko is the Head of Legal, Security & Investigations/Company Secretary-He has unrivalled experience in Banking & Finance. Mr. Ouko acquired extensive conventional commercial banking experience in Key departments such as - Operations, Customer Service and Credit Departments and in the legal practice having acquired over 14 years' experience in Commercial Law, Conveyancing Law, Banking Law Legal Advisory Services in Commercial Banks in Kenya and In East Africa including: Diamond Trust Bank of Kenya Limited, Kenya Post Office Savings Bank, Chase Bank of Kenya Limited, Equity Bank Kenya Ltd., Equity Bank South Sudan Limited and Co-operative Bank of South Sudan Limited.

Mr. Ouko holds a Master of Laws and Bachelor of Laws from the University of Nairobi. He has also earned reputable certifications key among them Certified AML Specialist by INTERFIMA (2016), Certified AML Specialist by INTELLISYS (2016) and Certified Systems Auditor by BERE A VERITAS.

SENIOR MANAGEMENT



Ms. Anne Waiyego Karanja
Managing Director



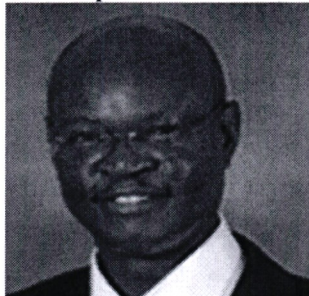
Mr I.J.S Obuon
Chief Operations Officer



Simon Njoroge
Head Banking services



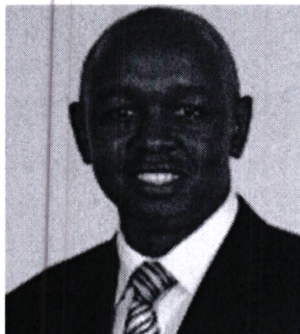
Jacinta Kasingiu
Head Special Projects



Henry Kenozwa Omumia
Head Information and
Communication Technology



Hannington Ouko
Head Legal/ Company Secretary



David Gatawa
Head Marketing & Business
Development



Thomas K. Bett
Head Human Resource
Administration & Property
Management



Evelynne Tsimanji Madigu
Head Finance & Accounting



Lydia Alum
Head Audit



Ms. Sabina Oyatsi
Head Human Resource, Special Projects

CORPORATE INFORMATION

Kenya Post Office Savings Bank (Postbank) is established under an Act of Parliament CAP 493B of the laws of Kenya, and is domiciled in Kenya. The address of the registered office of the Bank is:

Postbank House
16th Banda Street
P. O. Box 30311 00100,
Email: md@postbank.co.ke
Website: www.postbank.co.ke
NAIROBI-KENYA

Postbank is primarily engaged in the mobilization of savings for national development and operates under the Kenya Post Office Savings Bank Act Cap 493B. In addition, the Bank offers other financial services such as remittance, collections and disbursement services.

Principal Banks

Kenya Commercial Bank Ltd
Kencom House – 6th Floor
P.O Box 48400 - 00100
Tel: +254-020-3270000
NAIROBI

National Bank of Kenya Ltd
Harambee Avenue branch
P.O Box 72866-00200
Tel: +254-020-2828000
NAIROBI

Citibank, N.A.
P.O Box 30711-00100
Upper Hill Road
NAIROBI

Independent Auditor

Auditor- General
Office of Auditor General
Anniversary Towers, University Way
P.O.Box 30084-00100
NAIROBI

CORPORATE INFORMATION [Continued]

Principal Legal Advisers

Kale Maina & Bundotich Advocates
Teleposta Towers, 13th Floor, Kenyatta Avenue
P.O Box 10674-00100

NAIROBI

Kimaru Kiplagat Advocates
National Bank Building, 1st Floor, Uganda Road
P.O Box 5025-30100

ELDORET

Cherono & Co. Advocates
Hazina Towers, 8th Floor, Monrovia Street
P.O. BOX 4007-00100

NAIROBI

Kantai & Co. Advocates
Bruce House, 10th Floor, Standard Street
P.O. BOX 34247

NAIROBI

Macharia-Mwangi & Njeru Advocates
ACK Garden Annex, 6th Floor, 1st Ngong Avenue
P.O. BOX 10627-00100

NAIROBI

CHAIRMAN'S STATEMENT

I am pleased to present the Annual Report and Financial Statements of Kenya Post Office Savings Bank (Postbank) for the year ended 31st December 2017.

REVIEW OF ECONOMIC PERFORMANCE

Global and Regional Economy

The global economy is estimated to have expanded by 2.9 per cent in 2016 with growth in advanced economies expanding by 2.1 per cent in 2016 compared to 1.9 per cent in 2015.

Globally, there is a pickup in manufacturing and trade, rising market confidence and stabilization of commodity prices, allowing growth to resume in commodity-exporting emerging market and developing economies.

In the year 2016, real GDP in the East Africa Community (EAC) is estimated to have grown by 6.1 per cent compared to 5.8 per cent growth in 2015. The growth was fueled by public infrastructure investment, buoyant private consumption and low oil prices.

Growth in Sub-Saharan Africa is recovering, supported by modestly rising commodity prices strengthening external demand, and the end of drought in a number of countries. Security threats have subsided in several countries.

Growth in Sub-Saharan Africa is forecast to pick up to 2.6 percent in 2017 and to 3.2 percent in 2018, predicated on moderately rising commodity prices and reforms to tackle macroeconomic imbalances.

Kenyan Economy

Kenya's economic growth is estimated to have decelerated to 4.4 per cent in the third quarter of 2017 compared to 5.6 per cent in a similar period of 2016. During quarter three 2017, the macroeconomic fundamentals remained largely stable and supportive of growth. However, uncertainty associated with political environment coupled with effects of adverse weather conditions slowed down the performance of the economy. As a result, most sectors of the economy posted slower growths compared to the same quarter of 2016.

The African Development Bank (ADB) projects a positive outlook in 2018 and projects a growth of 6.5 per cent in 2018. The National Treasury projects similar growth rates of over 6 per cent in 2018.

Inflation

Kenya's inflation slowed down to 4.5% in December 2017. Consumer prices in Kenya increased 4.5 percent year-on-year in December of 2017, easing from a 4.7 percent rise in the previous month. It was the lowest inflation rate since May 2013, as prices went up softer mainly for food and housing and utilities.

The Exchange rate

The Kenyan Shilling remained largely stable in the year with the exception of the period around the presidential poll re-run date of 26th October and the period immediately after due to political

CHAIRMAN'S STATEMENT (continued).

jitters. To its credit, the Central Bank has always stepped in to calm markets and maintain stability through direct intervention by selling off dollars from its reserves. Improved diaspora remittances and tourism receipts have contributed to the cushioning of the central Bank's reserves and its ability to intervene in the exchange rate.

Interest rates

Yields on benchmark Government Treasury Bills were stable during the quarter. The rates oscillated between 7.89% and 8.56% for the 91-day Treasury Bill, 10.467% and 10.568% for the 182-day Treasury Bill and 10.599% to 11.053% for the 364-day Treasury Bill. Stability in the interest rate regime reduces uncertainty in decision making and ultimately reduces the premium when pricing risk.

Year 2017 Results

During the year 2017, Postbank's net operating income reduced by 9.39% from Kshs. 798,464,083 in 2016 to Kshs.723,482,201 in 2017. On customers' deposit, the Bank achieved Kshs.18.901 billion against a target of Ksh.19.840 billion which translates to 95.26% achievement. The Bank's deposit mobilisation efforts are negatively affected by lack of credit.

Corporate Governance

The Board continued to play its role within the tenets of good governance principles. However, for the big part of the year 2017, the Board was not fully constituted, hence posing a big challenge especially in business policy formulation and corporate oversight. As a matter of fact the advisory committees namely: Audit and Risk, and Human Resources only met once whereas Strategy and Development committee did not meet.

Outlook for 2018

According to the World Bank, near-term GDP growth is expected to decelerate to 5.5% in 2017 because of drought, weak credit growth, security concerns, and a rise in oil prices. Medium-term GDP growth should rebound to 5.8% in 2018 and 6.1% in 2019 respectively, depending on the completion of ongoing infrastructure-projects, the resolution-of slow credit growth, and the strengthening of the global economy and tourism.

In the long-term, the adoption of prudent macroeconomic policies will help safeguard Kenya's robust economic performance. This includes the implementation of fiscal and monetary prudence and lowering the deficit down to 4.3% by FY19/20, as per the Medium Term Fiscal Framework. Fiscal consolidation needs to avoid compromising public investment in critical infrastructure key to unlocking the economy's productive capacity.

CHAIRMAN'S STATEMENT (continued).

Interest Rates -

Stability in the interest rate regime was the theme in the year 2017. Yields on benchmark Government Treasury Bills oscillated between 8.00% to 8.8% for the 91 day Treasury Bill, 10.31% to 10.58% for the 182 day Treasury Bill and 10.7% to 11.13% for the 364 day Treasury Bill. The Central Bank has succeeded in maintaining a low and stable interest rates regime partly aided by the interest rates cap which has seen Commercial Banks take up Government Securities instead of private sector lending. Stability in the interest rate regime reduces uncertainty in decision making and ultimately reduces the premium when pricing risk.

Inflation

Inflation is expected to come under pressure in the year with the possibility of breaching the upper limit target of 7.5%. The failed short rains have led to a drought and this is expected to adversely affect

food production leading to a spike in the price of food, which is a major component in determining the level of inflation. Additionally, energy prices have trended upwards in the last month of 2016 and January 2017 and this is expected to further put inflationary pressures in the economy.

Exchange Rate

The global strengthening of the dollar is expected to put pressure on the local currency as investors exit the Kenyan market wary of booking exchange losses on their investments. The drought in the country is expected to adversely impact agricultural production of key exports such as tea reducing the expected dollar receipts on the sale of the crop. Less dollar receipts from tea will further put a strain on the local exchange rate. The Bank will continue to carefully scan the business environment and align its strategies accordingly to take advantage of emerging opportunities as well as address risks that may impact on its business model.

Strategic Planning

In the year 2017, the Bank continued the implementation of its five (5) year strategic Plan – 2016-2020. A midterm review of its Action Plan 2017 was carried out in 2017 and also the development of the Action Plan 2018 was undertaken. This formed the basis of performance contracting with the Government of Kenya for the year 2018.

Strategic Partnerships

The Bank continues to maintain strategic partnerships with key organizations which allows for Postbank to network, gain knowledge and share experiences with other members within the partnerships. These are:

1. Association of Savings Bank of East Africa (ASBEA)
2. World Savings Banks Institute (WSBI)
3. Association of Micro- Finance Institutions (AMFI)
4. Kenya Bankers Association (KBA)

CHAIRMAN'S STATEMENT (continued).

Association of Savings Bank of East Africa (ASBEA) 15th Annual Meeting

The Bank hosted the ASBEA Annual meetings in Nairobi from the 29th to 30th November 2017. The theme of the meetings and the conference was “*Transforming Savings Bank Customer Experience through Digital Innovation*” and participants’ members were from the three Savings Banks in East Africa and invited guests and presenters. The conference was a success.


During the Conference, various presentations that have an impact on the bank’s operations were discussed. These included: *Rethinking the Future of Banking Amid Digital Disruptions; The Effect of Cyber Security, Challenges and Mitigation Strategies in the Banking Sector; The Impact of Interest Capping Law in Kenya, Challenges and Responses by Financial Institutions; Effective Leadership in Digital disruption; Engaging Human Capital In Change Management: A TPB Bank Case Study and Customer Centricity: The last mile in the Financial Inclusion journey.*

During the 6th Board of Trustees and the 15th Annual General Meetings, a number of items were transacted. These included consideration of the next steps in the ICT Convergence project for the member banks, joint training programmes for the member banks in the year 2018, offering of Consultancy and Training services as a way of generating income; strategic plan for the year 2018 and approval of the financial budget for the year 2018.

Overall the meetings especially the Conference provided more insights on how the banks should respond to emerging environmental and operational issues.

Appreciation

I would like to convey my sincere appreciation to the Government, our esteemed customers and business partners for their continued support. I also wish to thank the management and staff for their dedication to service.



.....
MR. LAWRENCE TANUI.....

DIRECTOR

29TH MARCH 2018

MANAGING DIRECTOR'S STATEMENT

I wish to present the Bank's Annual Report and the Financial Statements for the year ended 31st December 2017.

Financial Performance

Postbank's financial performance (profit / loss) for the period ended 31st December, 2017 was a loss of Kshs.1.364 billion recording a negative growth of 5.98% from 2016 figure of Kshs.1.287 billion.

Total assets decreased by 2.68% to stand at Kshs 13.361 from Kshs. 13.738 billion in the financial year 2016, mainly due to decrease in assets and reserves. Customer deposits increased to stand at Kshs 18.901 billion in the financial year from Kshs 17.945 in year 2016 which is a 5.33% positive change.

The decline in performance was occasioned by:

- Lack of credit which has resulted to accounts falling into dormancy. A number of accounts were closed in the year due to lack of activity for over seven years and the accounts had zero balance.
- Reduced revenues due to reduced active accounts.
- Reduces investment due to declining deposits.

Affiliations

During the Year 2017, the Bank maintained its affiliations with various organisations including but not limited to the World Savings and Retail Banking Institute (WSBI), Association of Savings of Banks of East Africa (ASBEA) and the Association of Micro Finance Institutions (AMFI) Kenya; Kenya Bankers Association (KBA) and The Kenya Banking Institute (KBI).

The Bank continued to participate in meetings, seminars and other activities geared towards business growth. Specifically, the WSBI supported the Bank in the following activities;

- Customer centricity training
- Research on causes of dormancy of accounts with youth accounts
- Strategies to handle dormancy
- Global Money Week
- Development of the Mchama platform for group savings
- Research on enhancing the potential of the Postbank Mashinani agency

For ASBEA, the Bank participated in the Annual General Meetings in which the ASBEA Strategic Plan 2016-2020 was discussed and the the 2018 Action plan developed. AMFI provided capacity training opportunities for the Bank while KBA sensitised the Bank on the various advocacy assignments that the institution is undertaking.

In December 2017, the Bank negotiated its annual performance contract with the Government of Kenya for the financial year 2018. The contract was then cascaded to all levels within the Bank. Quarterly performance monitoring and evaluation was carried out.

MANAGING DIRECTOR'S STATEMENT (continued).

Performance contracting

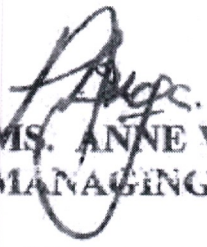
Towards the end of the year 2017, the Bank started its performance contracting process with the Government of Kenya for the year 2018. The contract was negotiated with the National Treasury and vetted early in the year 2018 by the Performance Management and Coordination Office, under the Executive Office of The President.

Strategic Partnerships

The Bank continues to maintain strategic partnerships with key organizations which allow Postbank to network, gain knowledge and share experiences with other members within the partnerships. These are: World Savings and Retail Banks Institute (WSBI); Association of Savings Bank of East Africa (ASBEA); Association of Micro- Finance Institutions (AMFI); and the Kenya Bankers Association (KBA).

Business partnerships

During the year 2017, the Bank continued to enter into various business partnerships to grow the Bank's business. In the year, the Bank entered into a partnership with the National Youth Service (NYS) to carry out financial literacy and also facilitate stipend payments to the NYS graduands who are posted to various parts in the country. We also partnered with additional water companies during the course of the year.


MS. ANNE W. KARANJA
MANAGING DIRECTOR

29TH MARCH 2018

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31ST DECEMBER 2017

The Board of Directors have the pleasure to submit the annual report and audited financial statements for the year ended 31st December 2017 in accordance with the International Financial Reporting Standards, which discloses the state of affairs of the Bank.

Principal activities

The principal activities of the Bank during the year under review were primarily savings education and financial literacy, collection of funds from private and public enterprises and disbursement of funds for Government pensions and salaries in accordance with KPOSB ACT CAP 493B.

Results

The results for the year are as set out on pages 25 to 65

Directors

The Directors who served during the year to the date of this report were: -

| Name | Title | Appointment Date | Retirement Date |
|---------------------------|--|------------------|---------------------------------|
| Hon. Fred Chesebe Kapondi | Chairman | 10-01-2014 | 31 st , January 2017 |
| Mr. Henry K Rotich, EGH | CS, National Treasury | May 2013 | In Service |
| Mr. Nzomo Mutuku | Alt. Representing CS The National Treasury | 24-09-2014 | 30 th , May 2017 |
| Dr. Urbanus Kioko | Director | 19-01-2015 | In service |
| Ms Jane Moronge | Director | 02-10-2015 | May 2017 |
| Mr. Lawrence Tanui | Director | 02-10-2015 | In Service |
| Ms Anne W. Karanja | Managing Director | 01-07-2014 | In service |

The Auditor General is responsible for the statutory audit of Postbank in accordance with the Article 229 of the Constitution of Kenya and Public Audit Act 2015 for the period ended 31st December 2017.

By order of the Board.



COMPANY SECRETARY

29TH MARCH 2018

CORPORATE GOVERNANCE STATEMENT

Postbank is committed to the standards of corporate governance as set by the Government for the public sector from time to time and the Central Bank of Kenya on specific services offered by Postbank.

The Board of Directors is responsible for the long term strategic direction for profitable growth of the Bank while being accountable to the shareholder by ensuring that Postbank complies with the laws and the highest standards of corporate governance and business ethics.

The Directors attach great importance to the need to conduct the business and operations of Postbank with integrity and in accordance with generally accepted corporate practice and endorse the internationally developed principles of good corporate governance.

Board of Directors

The Board is made up of six (6) Directors of whom 5 are non-executive including the Chairman. The term for the Chairman ended on 10th January 2017. One of the other Director resigned in April 2017 and the Alternate Director was appointed to Head another Government body in April 2017. The Board was therefore not fully constituted for the rest of the year since there were no replacements.

Directors are given appropriate and timely information so that they can maintain full and effective control over strategic, financial, operational and compliance requirements. The day-to-day running of Postbank has been delegated to the Managing Director. The Board retains responsibility for establishing and maintaining the internal control over the strategic, financial, operational and compliance issues. The Board is responsible of ensuring succession planning and facilitates recruitment of the Managing Director.

Despite not having a fully constituted Board the Bank is complying with the Mwongozo “the code of governance for state corporations” and all the Directors have undergone training on the code organised by the State Corporation Advisory Committee (SCAC).

Board Meetings

The Board of Directors meet on quarterly basis or as required. The Board is responsible for monitoring the implementation of Postbank’s planned strategy and reviewing it in conjunction with its financial performance. Specific reviews are also undertaken on operational issues and future planning. At the end of each financial year, the Board evaluates itself, the Managing Director and Senior Management Staff against targets that have been agreed at the beginning of the year. Due to lack of a fully constituted Board, we have had only one Board meeting in 2017.

Code of Ethics

Postbank is committed to the Public Officers Integrity and Ethics Act 2003, Leadership and Integrity Act 2012 and Kenya Anti-Corruption and Economic Crimes Act 2003.

Communication with Shareholder

Postbank is committed to ensuring that the shareholder and the Parliament are provided with full and timely information about its performance. This is usually done through the distribution

CORPORATE GOVERNANCE STATEMENT [Continued]

of the Bank's quarterly reports to the Inspectorate of State Corporations and Ministry of Finance and specifically the Annual reports to the Clerk of the Parliament for distribution to the Members of Parliament. Postbank

is in compliance with its obligations under the KPOSB Act, State Corporations Act and Central Bank of Kenya guidelines relating to remittance services together with other Guidelines issued by the Government.

Directors' Emoluments and Loans


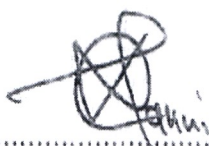
The aggregate amount of emoluments paid to Directors for services rendered during the Year 2017 is disclosed in Note 22 to the Financial Statements. There were no loans given to sitting Directors at any time during the year.

Board and Board Committees Attendance

The following table gives the record of Postbank's Board and Committee Meetings for the year ended December 31st 2017.

BOARD ATTENDANCE REGISTER 2017

| Type of Meeting | No. of Meetings | Hon. Fred Kapondi | Dr. Urbanus Kioko | Mr. Nzomo Mutuku | Ms. Jane Moronge | Mr. Lawrence Tanui | Ms. Anne Karanja |
|--|-----------------|-------------------|-------------------|------------------|------------------|--------------------|------------------|
| Main Board Meeting | 1 | - | 1 | 1 | 1 | 1 | 1 |
| Special Board Meeting | 2 | 1 | 2 | 2 | 1 | - | 2 |
| Audit and Risk Board Committee | 1 | N/A | 1 | 1 | N/A | 1 | N/A |
| Staff Board Committee | 5 | N/A | 5 | N/A | 2 | 3 | 5 |
| Strategy and Development Board Committee | 1 | N/A | N/A | 1 | 1 | 1 | 1 |
| Ad hoc Staff Committee | 1 | N/A | N/A | N/A | N/A | 1 | N/A |
| Attendance % | 100% | 100% | 100% | 100% | 55% | 64% | 100% |

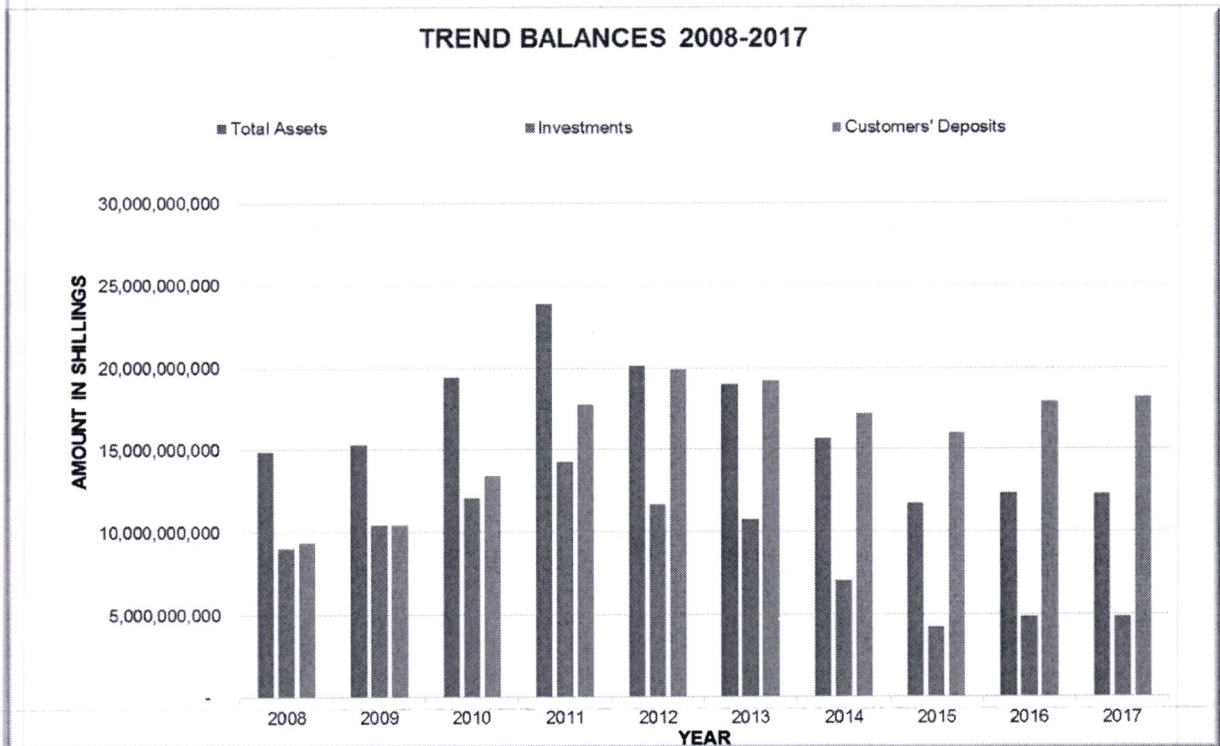

MANAGING DIRECTOR

DIRECTOR29TH MARCH 2018

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Performance

The financial performance (profit / loss) for the period ended 31st December, 2017 increased to Kshs.1.364 billion loss recording a negative growth of 5.98% from 2016 figure of Kshs.1.287 billion. Total assets decreased by 2.68% to stand at Kshs 13.361 billion from Kshs. 13.738 billion in the financial year 2016, mainly due to decrease in assets and reserves. Customer deposits increased to stand at Kshs 18.901 billion in the financial year from Kshs 17.945 in year 2016 which is a 5.33% positive change as given in trend analysis below.



Compliance with Statutory Requirement

During the period under review, the Bank honoured all its statutory obligations by remitting all required deductions within the statutory time line.

Strategic Plan 2016 -2020

In the year 2017, the Bank commenced on the implementation of the second year of its 5 year strategic Plan – 2016-2020. During the year, the Bank carried out a midterm review of its Action Plan 2017 and also developed the Action Plan for the year 2018. This Strategic Planning process was followed by a budgeting process for the year 2018. The Action Plan and Budget 2018 together formed the basis of performance contracting with the Government of Kenya for the year 2018.

Major Risk Facing Postbank

The major risk facing Postbank is lack of one stop shop banking solution for customers

MANAGEMENT DISCUSSION AND ANALYSIS (continued)

Compared to the competition. The Bank is a Savings Bank and not a lender, thus the customers find it easier to save where the Financial Institution can provide loans to assist them grow business, buy key assets and payment of school fees among others. This has led to shrinking of the customer deposit base, dormant accounts and as a result, led to depletion of the Bank's capital base and losses.

The Board and the management have been in consultation with the Government through the National Treasury with a view to injecting capital to defray the accumulated losses as provided in the Kenya Post Office Savings Bank Act, cap 493B, section 13(i).

The management is also addressing areas of cost management and through staff rationalisation and closing unprofitable branches. Five (5) branches were closed during the year under review. Customers will still be served through the Mashinani Agency Network, Mobile Banking and Internet Banking. Management is enhancing business Partnership's with the Government and Private sector especially for disbursement of Government Social funds and stipend, salaries and wages.

The National Treasury approved the sale of the Postbank Training School in Muthaiga North in December 2016 to partly fund the staff restructuring. This will reduce the cost income ratio. The sale process has commenced and we are hoping to conclude by end of June 2018 subject to receiving a responsive bid.

2017 CORPORATE SOCIAL RESPONSIBILITY (CSR) STATEMENT

INTRODUCTION

Postbank is committed to growing its business while ensuring that delivery of services is done in an ethical and socially responsible manner. The Bank considers the interests of the communities and strives to maintain the highest standards of ethical conduct and corporate responsibility in service delivery.

Over the years, the Bank has embraced Corporate Social Responsibility (CSR) in an effort to give back to the community. The Bank acknowledges that CSR is fundamental to our culture and core values. We encourage staff to conduct their affairs in a responsible manner as espoused in the Bank's corporate values.

The key focus of the Bank's Corporate Social Responsibility are:

- Education
- Health
- Financial Literacy
- Environment

In 2017, Postbank supported different causes aligned to our strategic direction and participated in a range of community activities as detailed below.

EDUCATION

The Bank supports initiatives that promote conducive learning environment to students from all spheres. The Bank strongly believes that education is an investment for the country's future.

Donation of Lecture Chairs to Kenya Medical Training College – Kilifi

Towards this end, the Bank donated lecture chairs to students of the Kenya Medical Training College.

In its latest effort to participate in causes that impact the society positively, the Bank was quick to respond to the schools' call for aid to add lecture chairs to accommodate the increasing number of students.

Postbank Supports the Coin-Chain- for Education Activity

In the spirit of achieving our mandate of mobilizing savings for national development, Postbank also sponsored "The JA Coin – Chain" that sought to raise funds for e-learning toolkits to support entrepreneurship and financial skills training to 50 secondary schools.

During the Coin Chain for education activity, Postbank was recognized as the most creative organization. The event provided a great team-building opportunity for staff, provided an opportunity to showcase Postbank products as well as exposure to potential customers.

HEALTH

The bank through its CSR arm has continued to push its shared growth agenda through supporting various health initiatives in the country.

2017 Mater Heart Run and Zambezi Hospital Cancer Walk

Postbank employees participated in "Mater Heart Run 2017", a charity event, which was hosted by the Mater Hospital in an effort to raise funds to assist children from families who cannot afford cost of cardiac surgery. The Bank believes that a healthy nation is a wealthy nation.

CORPORATE SOCIAL RESPONSIBILITY (CSR) STATEMENT [Continued]

The Bank also partnered with Zambezi Hospital to increase awareness on cancer as it has been identified as a silent killer in our communities especially because of low level of awareness, late

diagnosis and lack of affordable facilities for cancer management. The event entailed a 5km cancer walk dubbed “*Relentless in our commitment to fight Cancer together*” in fighting the cancer endemic.

FINANCIAL LITERACY

Postbank believes that a higher level of financial literacy and savings education not only enriches the life of the individual but also contributes to healthy economic growth in the society. We believe that if Kenyans are empowered with financial knowledge, they are better positioned to make sound financial decisions and consequently increase the national savings rate.

During the year, the Bank leveraged on opportunities for promoting financial education. The Bank has put financial inclusion high on its priority list and believes that access to finance is vital for poverty alleviation and social harmony. The ability to save and invest is an important component of poverty reduction and self-empowerment.

2017 Global Money Week


The annual celebration of the Global Money Week in March consists of a series of activities held across the world by the partners and stakeholders of the Child and Youth Finance Movement (CYFI). These activities are geared towards engaging children, youth and their communities in learning about financial education and financial inclusion. For the fifth year in a row, the Global Money Week, themed “Take Part, Save Smart!” was celebrated at Postbank in coordination with the Central Bank of Kenya. 2017 Global Money Week was marked from 27th March to 4th April.

Group Based Financial Literacy Programmes

The Bank also partnered with various organizations in pursuit of enhancing financial literacy. Among these include Cap-Yei and formal savings groups. This is in an effort to boost financial literacy levels to the unbanked and underserved Kenyans who may be unfamiliar with the fundamentals of personal financial management. The Bank has undertaken initiatives through grass root savings education to ensure that this knowledge is passed on to them through participation in various events.



DIRECTOR.....
29TH MARCH 2018


MANAGING DIRECTOR

STATEMENT OF DIRECTORS RESPONSIBILITIES

The State Corporations' Act requires the Directors to prepare financial statements for each financial year, which gives a true and fair view of the state of affairs of the Bank as at the end of the financial year and of the operating results for that year. It also requires the Directors to ensure that the entity keeps proper accounting records which disclose with reasonable accuracy the financial position of the entity. The Directors are also responsible for safeguarding the assets of the entity.

The Directors are responsible for the preparation and presentation of the entity's financial statements, which give a true and fair view of the state of affairs of the entity for and as at the end of the financial ear (period) ended on 31st December 2017.

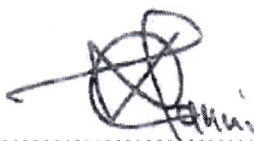
This responsibility includes: (i) maintaining adequate financial management arrangements and ensuring that these continue to be effective throughout the reporting period; (ii) maintaining proper accounting records, which disclose with reasonable accuracy at any time the financial position of the entity; (iii) designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of the financial statements, and ensuring that they are free from material misstatements, whether due to error or fraud; (iv) safeguarding the assets of the entity; (v) selecting and applying appropriate accounting policies; and (vi) making accounting estimates that are reasonable in the circumstances.

The Directors accept responsibility for the entity's financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Financial Reporting Standards (IFRS), and in the manner required by the PFM Act, 2012 and (the State Corporations Act).

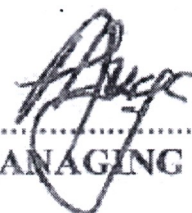
The Directors are of the opinion that the Postbank's financial statements give a true and fair view of the state of Postbank's transactions during the financial year ended December 31st, 2017, and of the Bank's financial position as at that date. The Directors further confirm the completeness of the accounting records maintained for the Bank, which have been relied upon in the preparation of the Bank's financial statements as well as the adequacy of the systems of internal financial control.

Approval of the financial statements

The Bank's financial statements were discussed and approved by the Management during the January monthly departmental meeting on 16th January 2018 and signed on its behalf by:



.....
DIRECTOR


.....
MANAGING DIRECTOR

REPUBLIC OF KENYA

Telephone: +254 20 317110
Fax: +254 20 317452
E-Mail: oag@oagkenya.go.ke
Website: www.kenao.go.ke

29th MARCH 2018



P.O. Box 30084-00100
NAIROBI

OFFICE OF THE AUDITOR-GENERAL

REPORT OF THE AUDITOR-GENERAL ON KENYA POST OFFICE SAVINGS BANK FOR THE YEAR ENDED 31 DECEMBER 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kenya Post Office Savings Bank set out on pages 25 to 62, which comprise the statement of financial position as at 31 December 2017, statement of profit or loss and other comprehensive income, statement of changes in equity, statement of cash flows and statement of comparison of budget and actual amounts for the year then ended, and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 35 of the Public Audit Act, 2015. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit.

In my opinion, except for the effects of the matters described in the Basis for Qualified Opinion section on my report, the financial statements present fairly, in all material respects the financial position of Kenya Post Office Saving Bank as at 31 December 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) and comply with the Kenya Post Office Savings Bank Act, 493B, Public Financial Management (PFM) Act, 2012 of the Laws of Kenya.

Basis for Qualified Opinion

1. Accounts Receivable

The statement of financial position reflects accounts receivable amount of Kshs.2,723,077,613 (2016 Kshs.2,873,129,934) and as disclosed under Note 34 to the financial statements. Included in this amount is Kshs.60,203,935 (2016 Kshs.50,618,767) on account of rent receivable from let out office space. Of the amount, Kshs.47,113,844 is owed by tenants who have since vacated the Bank's premises without the recourse as provisioned for in the lease agreements being exercised. The likelihood of the amount being collected is doubtful; adjustments necessary by way of provisions for the uncertainty have not been incorporated in the financial statements. In the circumstances, I am unable to confirm the fair statement of the accounts receivable.

Report of the Auditor-General on the Financial Statements of Post Office Savings Bank for the year ended 31 December 2017

2. Interest Expense

The statement of profit or loss and other comprehensive income reflects interest expense amount of Kshs.567,955,405 (2016Kshs.562,788,544) and disclosed under Note 15 to the financial statements. However, the interest expense ledger in support reflects a balance of Kshs.589,083,108 resulting in a variance of Kshs.21,127,703. Of the variance amount, management has not been able to render explanations for the variance of Kshs.4,853,513. In the circumstances, I am unable to confirm the accuracy of the reported interest expenses amount.

3. Encroached on Land without Title Deed

The statement of financial position indicates property and equipment balance of Kshs.1,714,988,172 as of statement date and disclosed under note 36(b) to the financial statements. Included in the balance, is parcel of land valued at Kshs.5,000,000 located in Dandora Phase II allotted to the Bank in 1993. Management is yet to obtain title deed to the land parcel. In addition, the land has not been fenced off, consequently it had been encroached by squatters as at the time of finalizing this audit. In the circumstances, the Bank's ability to access the land as and when it needs is doubtful.

4. Motor Vehicle without Log Book

Also included in the property and equipment balance is motor vehicles valued at Kshs.29,123,656. Included in the motor vehicle schedule is a Mercedes Benz registration number KAJ 078Y whose log book has not been issued to the Bank by Kenya Revenue Authority (KRA). This is despite the Bank having paid the requisite duty to register the vehicle in its own name in November 1997. In the circumstances, the accuracy and fair statement of property and equipment as of the statement date cannot be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Post Office Savings Bank in accordance with ISSAI 30 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Material Uncertainty Related to Going Concern

I draw attention to Note 1(e) (i) in the financial statements, which indicates that the Bank incurred a net loss of Kshs. Kshs.1,364,952,385 during the year ended 31 December 2017 (2016- 1,287,021,979), resulting into a reported accumulated deficit of Kshs.11,020,457,848 (2016- Kshs.9,599,351,297) and, as of that date, the Bank had a shareholder's equity deficit of Kshs.8,570,273,319 (2016- Kshs.7,171,095,436). These conditions, along with other matters as set forth in Note 1(e) (i), indicate that a material uncertainty exists that may cast significant doubt on the Bank's ability to continue as a going concern. My opinion is not qualified in respect of this matter.

Key Audit Matters

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

Other Matter

Prior Year Issues

1.0 Misstatement of Customer Savings and Deposits

The statement of financial position and note 38 to the financial statements reflects customer savings and deposits of Kshs.18,901,102,775 (2016 Kshs-17,944,664,853). As reported in the previous years, the customers savings and deposits then balance of Kshs.17,503,279,455 differed with the core banking system (CBS) balance of Kshs.17,515,289,289 by Kshs.12,009,845 as at 31 December 2014. This difference has remained unexplained over the years: 2015, 2016 and 2017.

2.0 GoK Pension Reserve Fund

The statement of financial position and note 40 to the financial statements indicates GoK Pension Reserve Fund asset of Kshs.74,381,227 (2016 liability- Kshs.183,942,031). As reported in the year 2016, the Pension Reserve Fund liability balance then of Kshs.Kshs.183,942,031 was made up of inactive accounts, accounts for deceased cases, Books on Hand (BOH) and suspected fraud cases over the years which should have been remitted back to the National Treasury upon confirmation. No explanations have been rendered on the account movements of Kshs.258,323,258 resulting into an asset closing balance as at 31 December 2017.

3.0 Interest Expense

As reported in 2014, interest expense for the year of Kshs.1,086,132,043 excluded CBS interest from Money Market of Kshs.656,264,332 and manual interest adjustments of Kshs.31,897,660.50 totaling to Kshs 688,161,992. Management subsequently explained the difference except for Kshs.3,137,356 which is outstanding to date. Consequently, the accuracy of the comparative shareholder's equity cumulative deficit of Kshs.7,171,095,436 as reflected in the financial statements could not be confirmed.

Report on Lawfulness and Effective in use of Public Resources

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matter described in the Basis for Lawfulness and Effectiveness in Use of Public Resources section of my report, I confirm that, nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way

Basis for Conclusion

High Employee Cost

Contrary to the provisions of the Public Finance Management Regulations 2015, that requires compensation of employees not to exceed 35% of revenue, the Banks employee expenses amounted to Kshs.1,192,722,658 or 91% of the total revenue of Ksh.1,313,796,114).

Report on Internal Controls Effectiveness, Governance and Risk Management Systems

As required by Section 7(1) of the Public Audit Act, 2015 I confirm that, nothing has come to my attention to cause me to believe that internal controls were not operating in an effective way.

Responsibilities of Management and those Charged with Governance for the Financial Statements

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

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

Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provision of Section 47 of the Public Audit Act, 2015.

Those charged with governance are responsible for overseeing the bank's financial reporting process.

Auditor-General's Responsibilities for the Audit

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution of Kenya. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement 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.

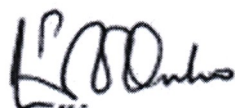
As part of an audit in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the bank's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entity or business activities to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

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

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

I am independent of Kenya Post Office Savings Bank in accordance with ISSAI 30 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya.



FCPA Edward R. O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

17 June 2019

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31ST DECEMBER 2017

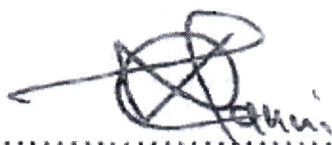
| | Notes | 2017 December Kshs | 2016 December Kshs |
|--|--------|-----------------------------|-----------------------------|
| Interest Income -In | 14 | 673,949,630 | 672,598,189 |
| Interest Expense | 15 | -567,955,405 | -562,788,544 |
| Net Interest Income | | <u>105,,994,225</u> | <u>109,809,645</u> |
| Fees and Commissions Income | 16 | 433,288,043 | 512,241,968 |
| Fees and Commissions Expense | 17 | -22,358,508 | <u>-20,005,767</u> |
| Net Fees and Commissions Income | | <u>410,929,535</u> | <u>492,236,201</u> |
| Net Trading Income | | <u>516,923,760</u> | <u>602,045,846</u> |
| Foreign Exchange Income | 18 | 84,979,563 | 76,675,558 |
| Other Operating Income | 19 | 121,578,878 | 119,742,679 |
| Net Operating Income | | 723,482,201 | 798,464,083 |
| Impairment loss on loans and advances | 20 | 13,000,000 | 20,000,000 |
| Employee Expenses | 21 | 1,192,722,658 | 1,152,426,662 |
| Board Expenses | 22 | 1,313,685 | 8,937,011 |
| Operating Expenses | 23 | 411,076,442 | 388,576,495 |
| Depreciation | 36(b) | 94,601,599 | 109,338,125 |
| Amortization Intangible Assets | 37 | 18,627,072 | 18,107,403 |
| Amortization for Bonds Trading Cost | 24 | 22,122,908 | 34,692,599 |
| Other Expenses | 25 | 334,970,222 | 353,407,767 |
| Total Operating Costs | | <u>2,088,434,586</u> | <u>2,085,486,062</u> |
| Profit/(Loss) before income tax | | -1,364,952,385 | -1,287,021,979 |
| Income tax expense * | | 0 | 0 |
| Profit/(Loss) for the Period | 26 | -1,364,952,385 | -1,287,021,979 |
| Disclosure Note | | | |
| Extra ordinary Income | 19 (b) | <u>62,076,491</u> | <u>10,975,743</u> |

*The Bank is exempted from paying corporate taxes as per the Income Tax Act Cap 470 First schedule Part 1.

STATEMENT OF FINANCIAL POSITION AS AT 31ST DECEMBER 2017


| | Notes | 2017 Kshs | 2016 Kshs |
|---|-------|------------------------|-----------------------|
| ASSETS | | | |
| Cash | 28 | 626,307,465 | 571,762,339 |
| Funds on Call and Short Notice | 29 | 35,579,852 | 33,608,117 |
| Investment in Treasury Bills and Bonds | 30(a) | 4,773,042,050 | 4,848,850,219 |
| Investment Property | 31 | 896,790,225 | 896,790,225 |
| Stocks | 32 | 12,993,081 | 16,798,864 |
| Other Investments | 33 | 4,124,001 | 3,692,401 |
| Accounts Receivables | 34 | 2,723,077,613 | 2,873,129,934 |
| Prepayments & Other Assets | 35 | 2,434,472,113 | 2,621,365,249 |
| GoK Pension Reserve Fund | 40 | 74,381,227 | 0 |
| Property and Equipment | 36(b) | 1,714,998,172 | 1,787,523,677 |
| Intangible Assets | 37 | <u>66,145,531</u> | <u>84,772,604</u> |
| Total Assets | | 13,361,911,330 | 13,738,293,629 |
| LIABILITIES | | | |
| Customer Savings and Deposits | 38 | 18,901,102,775 | 17,944,664,853 |
| Accounts Payables & Accruals | 39 | 3,031,081,874 | 2,780,782,184 |
| GoK Pension Reserve Fund | 40 | <u>0</u> | <u>183,942,031</u> |
| Total Liabilities | | 21,932,184,649 | 20,909,389,068 |
| SHAREHOLDERS' EQUITY | | | |
| Capital Grants | 41 | 12,907,037 | 12,907,037 |
| Revaluation Reserves | 11 | 2,388,250,796 | 2,388,250,796 |
| Change in Fair Value for Bonds AFS | 30(b) | 49,026,696 | 27,098,028 |
| Revenue Reserves | 12 | <u>-11,020,457,848</u> | <u>-9,599,351,297</u> |
| Total Shareholders' Equity | | -8,570,273,319 | -7,171,095,436 |
| Total Liabilities & Shareholders' Equity | | 13,361,911,330 | 13,738,293,629 |

The Financial statements on pages 27 to 29 were approved by the Management on 16th January, 2018 as a draft and signed on its behalf by:



DIRECTOR

29TH MARCH 2018



MANAGING DIRECTOR

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31ST DECEMBER 2017

| | Capital Grants | Revaluation Reserves | Change in Fair value | Revenue Reserves | TOTALS |
|---|-------------------|----------------------|----------------------|------------------------|-----------------------|
| | Kshs | Kshs | Kshs | Kshs | Kshs |
| At 1 st January 2016 | 30,570,479 | 2,388,250,796 | - | -8,342,815,180 | -5,923,993,905 |
| Profit/(Loss) for the year | | | | -1,287,021,979 | -1,287,021,979 |
| Additions during the year -AFS | | | 27,098,028 | | 27,098,028 |
| Transfer of grant utilised during the year (Note i) | -17,663,442 | | | | -17,663,442 |
| Prior year adjustment (Note ii) | | | | 9,889,533 | 9,889,533 |
| Prior year adjustment (Note iii) | | | | -1,293,876 | -1,293,876 |
| Prior year adjustment (Note iv) | | | | 1,086,209 | 1,086,209 |
| Prior year adjustment (Note v) | | | | 20,803,996 | 20,803,996 |
| At 31 st December 2016 | <u>12,907,037</u> | <u>2,388,250,796</u> | <u>27,098,028</u> | <u>-9,599,351,297</u> | <u>-7,171,095,436</u> |
| At 1 st January 2017 | 12,907,037 | 2,388,250,796 | 27,098,028 | -9,599,351,297 | -7,171,095,436 |
| Profit/(Loss) for the year | | | | -1,364,952,385 | -1,364,952,385 |
| Additions during the year -AFS | | | 21,928,668 | | 21,928,668 |
| Prior year adjustment (Note i) | | | | -2,211,052 | -2,211,052 |
| Prior year adjustment (Note ii) | | | | 17,778,929 | 17,778,929 |
| Prior year adjustment (Note iii) | | | | 44,297,562 | 44,297,562 |
| Prior year adjustment (Note iv) | | | | 692,944 | 692,944 |
| Prior year adjustment (Note v) | | | | -103,908,425 | -103,908,425 |
| Prior year adjustment (Note v) | | | | -12,804,123 | -12,804,123 |
| At 31 st December 2017 | <u>12,907,037</u> | <u>2,388,250,796</u> | <u>49,026,696</u> | <u>-11,020,457,848</u> | <u>-8,570,273,319</u> |

- (i) Prior year adjustment of Kshs.2,211,052 relates payment of audit fees to KENAO for period 2015 which was under budgeted.
- (ii) Prior year adjustment of Ksh.17,778,929 relates to receipts from ailing Institutions –Trust Bank during the year.
- (iii) Prior year adjustment of Ksh.44,297,562 relates to receipts from ailing Institutions – Postbank Credit Ltd during the year.
- (iv) Prior year adjustment of Ksh.692,944 relates to correction of overstated depreciation in year 2016.
- (v) Prior year adjustment of Ksh.103,908,425 relates to payment of Union staff members’ salary arrears in 2018 for three years and half i.e. from July 2013 to December 2016. Total salary arrears paid in January 2018 was Ksh.144,168,530 for period July 2013 to June 2017 hence the balance of Ksh 40,260,105 charged in the current year.
- (vi) Prior year adjustment of Ksh.12,804,123 relates to payment of Union staff members’ pension paid in 2018 for three years and half i.e. from July 2013 to December 2016. Current charge to the financial period 2017 Kshs. 4,965,931, hence total pension paid out Kshs. 17,770,054.

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31ST DECEMBER 2017

| CASH FLOWS FROM OPERATING ACTIVITIES | 2017 | 2016 |
|--|-----------------------|-----------------------|
| | Kshs | Kshs |
| Profit/(Loss) for the year | -1,364,952,385 | -1,287,021,979 |
| Adjustments for:- | | |
| Depreciation | 113,228,671 | 127,445,528 |
| Rental Income | -86,557,526 | -81,136,604 |
| Dividend income | | |
| Gain/ (Loss) on Disposal of Property and Equipment | | -242,768 |
| Appreciation/Diminution in value of quoted investments | -431,600 | 267,100 |
| Prior year adjustments | -56,154,166 | 30,485,862 |
| Operating profit/(loss) before working capital changes | -1,394,867,006 | -1,210,202,861 |
| (Increase)/ Decrease in Accounts Receivables & Prepayments | 336,945,458 | -647,752,205 |
| (Increase)/Decrease in stocks | 3,805,783 | 547,832 |
| Increase/(Decrease) in Accounts Payables & Accruals | 250,299,693 | 495,193,127 |
| Increase/(Decrease) Customer Savings and deposits | 956,437,922 | 1,955,415,176 |
| Increase/(Decrease) GoK Pension Reserve fund account | -258,323,258 | -20,406,654 |
| Net cash flows from operating activities | -105,701,408 | 572,794,415 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase/Sale of Property and Equipment | -21,383,150 | -110,707,980 |
| Write back on Depreciation | -692,944 | |
| Gain/ (Loss) on Disposal of Property and Equipment | 0 | 242,768 |
| Change in fair Value for Bonds AFS | 21,928,668 | 27,098,028 |
| Rental income | 86,557,526 | 81,136,604 |
| Dividend Income | 0 | 0 |
| Net cash flows from investing activities | 86,410,100 | -2,230,580 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Receipts from WSBI | 0 | -17,663,442 |
| Net cash flows from financing activities | 0 | -17,663,442 |
| Net increase in cash and cash equivalents | -19,291,308 | 552,900,393 |
| Cash and cash equivalents at the beginning of the year | 5,454,220,675 | 4,901,320,282 |
| Cash and cash equivalent at the end of the year (Note 42) | 5,434,929,367 | 5,454,220,675 |

**STATEMENT OF COMPARISON OF BUDGET AND ACTUAL AS AT 31ST DECEMBER
2017**

| | ACTUAL TOTAL Shs | BUDGET TOTAL Shs | VARIANCE TOTAL Shs | VARIANCE TOTAL % |
|--|------------------------|------------------------|--------------------------|------------------------|
| Interest income | 673,949,630 | 752,604,938 | -78,655,308 | -1 |
| Interest expense | -567,955,405 | -700,000,000 | 132,044,595 | -1 |
| Net interest income | 105,994,225 | 52,604,938 | 53,389,287 | 10 |
| Fees and commissions income | 433,288,043 | 820,819,581 | -387,531,538 | -4 |
| Fees and commissions expense | -22,358,508 | -36,341,923 | 13,983,416 | -3 |
| Net fees and commissions income | 410,929,535 | 784,477,658 | -373,548,123 | -4 |
| Net trading income | 516,923,760 | 837,082,596 | -320,158,836 | -3 |
| Foreign exchange income | 84,979,563 | 80,500,000 | 4,479,563 | 6 |
| Other operating income | 121,578,878 | 160,210,602 | -38,631,726 | -2 |
| Operating income | 723,482,201 | 1,077,793,198 | -354,310,999 | -3 |
| Impairment loss on loans and advances | 13,000,000 | 12,000,000 | 1,000,000 | 0 |
| Employee expenses | 1,192,722,658 | 1,067,839,137 | 124,883,521 | 12 |
| Board expenses | 1,313,685 | 5,944,000 | -4,630,315 | -7 |
| Operating expenses | 411,076,442 | 393,739,188 | 17,337,254 | . |
| Depreciation expenses | 94,601,599 | 132,064,200 | -37,462,601 | -28 |
| Amortisation cost- Intangible Assets | 18,627,072 | 30,446,283 | -11,819,211 | -3 |
| Amortisation cost- Treasury bonds. | 22,122,908 | 23,083,893 | -960,985 | - |
| Other expenses | 334,970,222 | 331,742,111 | 3,228,111 | 1 |
| Total Operating Costs | 2,088,434,586 | 1,996,858,811 | -82,454,203 | - |
| Profit before income tax | -1,364,952,385 | -919,065,613 | 453,923,243 | -4 |
| Income tax expense | | | | |
| Profit for the period | -1,364,952,385 | -919,065,613 | 453,923,243 | -4 |

The notes set out on pages 30 to 65 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

1. BASIS OF PREPARATION

a) Statement of Compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) and International Accounting Standards (IAS). The financial statements were authorised for issue by the Management on 16th January, 2018.

The financial statements comprise of statement of comprehensive income, statement of financial position, statement of changes in reserves, statement of cash flows, and notes.

b) Basis of Measurement

The financial statements have been prepared in compliance with International Financial Reporting Standards (IFRS) based on the historical cost convention. The bank has not revalued any property.

c) Functional and Presentation Currency

These financial statements are presented in Kenya shillings (Kshs), which is the company's functional currency.

Items included in the financial statements are measured using the currency of primary economic environment in which the entity operates i.e. Kenya shillings.

d) Use of Estimates and Judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, incomes and expenses.

The estimates and assumptions are reviewed on an ongoing basis. Revision to estimates are recognized prospectively:

e) Assumptions and Estimation of Uncertainties

i) Going concern

The Bank operates with the intention of being in business in the next 12 months and in the foreseeable future. The management runs the day to day activities by ensuring that assets are realized and liabilities honoured in the normal course of business. However, the Bank's future performance is dependent on restructuring and government support in defraying the incurred losses from the year 2012 to 2017 amounting to Kshs. (11,020,457,848) in accordance with KPOSB Act cap 493B section 13 (1).

Note 20- Impairment loss on deposits, loans and advances

Note 13- Recognitions and measurement of contingencies: Key assumption about the likelihood and magnitude of an outflow of resources

ii) Critical judgement in applying the entity's accounting policies

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including experience of future events that are believed to be reasonable under the circumstances.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

In accessing the need for collective loss allowances, management considers factors such as:

- Credit quality
- Portfolio size
- Concentrations
- Economic factors

Note 5- Depreciation of equipment and intangible assets. The Bank reviews the useful life of its property and equipment and intangible assets at the end of each financial period

2. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements have been applied consistently over the years.

a) Revenue Recognition

Income is recognised on an accrual basis.

i) Interest

Interest income and expense are recognised in the statement of comprehensive income using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently.

The calculation of the effective interest rate includes all fees paid or received, transaction costs, and discounts or premiums that are an integral part of the effective interest rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Interest income and expense presented in the statement of comprehensive income include:

- interest on financial assets and liabilities at amortised cost on an effective interest rate basis;
- interest on available-for-sale investment securities on an effective interest basis; and
- 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.

ii) Fees and commission income

Fees and commission income and expense are recognised on an accrual basis when the service has been provided. Fees and commission income 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, are recognised as the related services are performed.

b) Foreign currency transactions

Transactions in foreign currencies during the year are converted into Kenya Shillings at rates ruling at the transaction dates. Monetary assets and liabilities at the reporting date which are expressed in foreign currencies are translated into Kenya Shillings at rates ruling at that date.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

The resulting differences from conversion and translation are dealt with in the statement of comprehensive income in which they arise.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions if any. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined if there is any.

c) Employee benefits

The Bank operates a defined contribution scheme whose funds are held in a separate trustee administered and guaranteed scheme managed by an approved investment company. The pension plan is funded by contributions from the employees and the Bank. The bank's contributions are charged to profit or loss in the year to which they relate.

d) New standards, amendments and interpretations effective and adopted during the year.

i) *Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38)*

The amendments to IAS 38 Intangible Assets introduce a rebuttable presumption that the use of revenue-based amortisation methods for intangible assets is inappropriate. The presumption can be overcome only when revenue and the consumption of the economic benefits of the intangible asset are highly correlated, or when the intangible asset is expressed as a measure of revenue.

The amendments apply prospectively for annual periods beginning on or after 1 January 2016. The adoption of these changes did not have a significant impact on the financial statements of the Bank.

ii) *Disclosure Initiative (Amendments to IAS 1)*

The amendments provide additional guidance on the application of materiality and aggregation when preparing financial statements. The amendment applies for annual periods beginning on or after 1 January 2016 and early application is permitted. The adoption of these changes does not have a significant impact on the financial statements of the Bank.

iii) *Disclosure Initiative (Amendments to IAS 7)*

The amendments in Disclosure Initiative (Amendments to IAS 7) come with the objective that entities shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities.

The IASB defines liabilities arising from financing activities as liabilities "for which cash flows were, or future cash flows will be, classified in the statement of cash flows as cash flows from financing activities". It also stresses that the new disclosure requirements also relate to changes in financial assets if they meet the same definition. The amendments state that one way to fulfil the new disclosure requirement is to provide reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities.

Finally, the amendments state that changes in liabilities arising from financing activities must be disclosed separately from changes in other assets and liabilities. The amendments are effective for annual periods beginning on or after 1 January, 2017, with early application permitted. Since the amendments are being issued less than one year before the effective date, entities need not provide comparative information when they first apply the amendments.

The Bank is assessing the potential impact on the financial statements resulting from the application of IAS 7.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

iv) IFRS 9: Financial Instruments (2014)

On 24 July 2014 the IASB issued the final IFRS 9 Financial Instruments Standard, which replaces earlier versions of IAS 9.

This standard introduces changes in the measurement bases of the financial assets to amortised cost, fair value through other comprehensive income or fair value through profit or loss. Even though these measurement categories are similar to IAS 39, the criteria for classification into these categories are significantly different.

In addition, the IFRS 9 impairment model has been changed from an “incurred loss” model from IAS 39 to an “expected credit loss” model.

The standard is effective for annual period beginning on or after 1 January 2018 with retrospective application, early adoption permitted. The Bank is assessing the financial impact on the financial statements resulting from the application on Accounts receivable Note 34 and Prepayments and other assets Note 35 an exposure of Kshs 2,728,388,820 and 2,461,600,162.00 respectively.

v) IFRS 16: Leases

On 13 January 2016 the IASB issued IFRS 16 Leases, completing the IASB’s project to improve the financial reporting of leases. IFRS 16 replaces the previous leases standard, IAS 17 Leases, and related interpretations.

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer (‘lessee’) and the supplier (‘lessor’). The standard defines a lease as a contract that conveys to the customer (‘lessee’) the right to use an asset for a period of time in exchange for consideration.

A company assesses whether a contract contains a lease on the basis of whether the customer has the right to control the use of an identified asset for a period of time. The standard eliminates the classification of leases as either operating leases or finance leases for a lessee and introduces a single lessee accounting model. All leases are treated in a similar way to finance leases. Applying that model significantly affects the accounting and presentation of leases and consequently, the lessee is required to recognise:

- a) Assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A company recognises the present value of the unavoidable lease payments and shows them either as lease assets (right-of-use assets) or together with property, plant and equipment. If lease payments are made over time, a company also recognises a financial liability representing its obligation to make future lease payments.
- b) Depreciation of lease assets and interest on lease liabilities in profit or loss over the lease term;
- c) Separate the total amount of cash paid into a principal portion (presented within financing activities) and interest (typically presented within either operating or financing activities) in the statement of cash flows.

IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. However, compared to IAS 17, IFRS 16 requires a lessor to disclose additional information about how it manages the risks related to its residual interest in assets subject to leases.

The standard does not require a company to recognise assets and liabilities for

- (a) Short-term leases (i.e. leases of 12 months or less) and;
- (b) Leases of low-value asset.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

The new Standard is effective for annual periods beginning on or after 1 January, 2019. Early application is permitted insofar as the recently issued revenue Standard, IFRS 15 Revenue from Contracts with Customers is also applied.

The adoption of these changes will affect the amounts and disclosures of the Bank's financial statements. The Bank is assessing the potential impact on the financial statements resulting from the application of IFRS 16.

3. FINANCIAL ASSETS AND LIABILITIES

a) Recognition

The Bank initially recognises loans, advances, deposits and debt securities on the date at which they are originated.

Purchases and sales of financial assets are recognised on the trade date at which the Bank commits to purchase or sell the asset.

A financial asset or liability is initially measured at fair value plus (for an item not subsequently measured at fair value through profit or loss) transaction costs that are directly attributable to its acquisition or issue.

b) Classification

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

i) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management.

ii) Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money directly to a debtor with no intention of trading the receivable. These include advances to staff, Visa credit to customers and placements with other banks. Loans are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

iii) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. Were the Bank to sell other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available for sale. These include Treasury Bills, Treasury Bonds and Government Stock.

iv) Available-for-sale

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates or exchange rates. Purchases and sales of financial assets at fair value through profit or loss, held to

maturity and available for sale are recognised on trade-date, the date on which the Bank commits to purchase or sell the asset. Loans are recognised when cash is advanced to the

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

borrowers. Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership.

Available-for-sale financial assets and financial assets are carried at fair value through profit or loss. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of the financial assets category are included in the statement of comprehensive income in the year in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity should be recognised in profit or loss. However, interest calculated using the effective interest method is recognised in the statement of comprehensive income.

As per IAS 39, financial instruments are supposed to be classified as Held-to-maturity and Available- for-sale. However, the Bank has classified all its financial instruments as Held-to-maturity since the Bank has no intention of selling the instruments.

(v) *Identification and Measurement of Impairment of Financial Assets*

At each statement of financial position date, the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset than can be estimated reliably.

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

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would otherwise not consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

In assessing collective impairment, the Bank uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rate, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective interest rate. Losses are recognised in the statement

of comprehensive income and reflected in an allowance account against loans and advances. Interest on the impaired asset continues to be recognised through the unwinding of the

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

discount. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the statement of comprehensive income.

Impairment losses on available-for-sale investment securities are recognised by transferring the difference between the amortised acquisition cost and current fair value out of equity to the statement of comprehensive income. When a subsequent event causes the amount of impairment loss on an available-for-sale debt security to decrease, the impairment loss is reversed through the statement of comprehensive income.

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

(vi) Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Bank enters into transactions whereby it transfers assets recognised on its statement of financial position but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the statement of financial position. Transfers of assets with retention of all or substantially all risks and rewards include, for example, securities lending and repurchase transactions.

vii) Impairment for Non-Financial Assets

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the assets' recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups.

Impairment losses are recognised in the statement of comprehensive income. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro-rata basis.

viii) Budget Accounting Policy.

The bank uses Zero-based budgeting (ZBB). All expenses must be justified for each new period. The budgeting starts from a "zero base," and every function within an organization is analysed for its needs and costs. Budgets are then built around what is needed for the upcoming period. This allows top-level strategic goals to be implemented into the budgeting process by tying them to specific functional areas of the organization, where costs can be first grouped and then measured against previous results and current expectations. At the end of every month actual and budgeted amount is compared to obtain variances. The presentation of budget information in Financial Statements is done as per International Public Sector Accounting Standard (IPSAS) 24

4). FINANCIAL RISK MANAGEMENT

(a) Principles

Postbank faces various types of risks which arise from its day to day operations as a financial institution. The Board of Directors and Management therefore devote a significant portion of

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

their time to the management of these risks. The mainstay of effective risk management is the identification of significant risks, the quantification of the Banks's risk exposure, actions to limit risk and the constant monitoring of risk.

The overarching aim of risk management is to ensure that all risks assumed in the course of the Bank's business are recognized early on and mitigated by effective risk management. Successful risk management is recognized as a pre-condition for the sustained growth and success of the Bank. Risk management and monitoring are implemented via the Bank's risk management and risk control process and the organization structure corresponds to prudent Risk Management Guidelines. In order to ensure continuous improvement of risk management at all times the following key risk principles have been adopted and are applied;

- The Board of Directors assumes the ultimate responsibility for the level of risks taken by the Bank and is responsible to oversee the effective implementation of the risk strategies.
 - The organizational risk structure and the functions, tasks and powers of the employees, committees and departments involved in the risk processes are continuously being reviewed to ensure clarity of their roles and responsibilities.
 - Risk issues are taken into consideration in all business decisions. Measures are in place to develop risk-based performance measures and this is being supplemented by setting risk limits at the overall Bank and divisional levels, as well as by enforcing consistent operating limits for individual business activities.
 - Risk management is increasingly being linked to management processes such as strategic planning, annual budgeting and performance measurement.
 - Identified risks are reported in a transparent and timely manner and in full to the responsible senior management.
 - Appropriate and effective controls exist for all processes entailing risks.
- All these principles are enshrined in the Bank's risk management policy. The section below provides the various risks faced by the Bank and describes the methods used by management to control risk. The most important types of financial risks to which the Bank is exposed are credit risk, liquidity risk and market risk mainly interest risk and operational risk.

(b) Credit risk

Credit risk is the current or prospective risk to earnings and capital arising from an obligor's failure to meet the terms of any contract with the bank or if an obligor otherwise fails to perform as agreed.

(i) Management of Credit Risk

The Bank is subject to credit risk through its lending and investing activities. Considerable resources, expertise and controls are devoted to managing it and comprehensive strategies, policies and procedures have been developed to effectively manage this risk. The Bank's primary exposure to credit risk arises through its advances to employee and Visa credit to customers. Credit risk ratings are assigned to customers to enable the bank to establish the risk and enable credit decisions to be undertaken within acceptable risk appetite threshold through its credit policy. At the management level there, is a credit risk department staffed with highly skilled personnel who ensure credit risk are identified and mitigated. Within this department

there are debt collecting officers who follow up on bad loans.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(ii) *Write-off Policy*

The Bank writes off a loan / security balance (and any related allowances for impairment losses) when management determines that the advances / securities are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower financial position such that the borrower can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

(c) *Liquidity Risk*

Liquidity risk is the current or prospective risk to earnings and capital arising from the institution's failure to meet its maturing obligations when they fall due without incurring unacceptable losses.

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

The Bank has access to a diverse funding base. Funds are raised mainly from deposits.

Exposure to liquidity Risk

The key measure used by the Bank for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets are considered as including cash and cash equivalents and investment securities for which there is an active and liquid market less any deposits from banks, other borrowings and commitments maturing within the next month.

The board has approved a policy to effectively manage liquidity at all times to meet depositors demand, and unexpected outflow. The investment undertakes statement of financial position liquidity and scenario analysis as per the policy on bi-monthly basis.

The bank strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with range maturities, in addition the bank holds a portfolio of liquid assets as part of its liquidity risk management strategy.

(d) *Market Risk*

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

(i) *Management of market Risk*

Overall responsibility for management of market risk rests with a management committee of the Bank, the Asset and Liability Committee (ALCO). The risk department is responsible for the development of detailed market risk management policies (subject to review and approval by ALCO) and for the day to day implementation of those policies. Regular monitoring of Postbank's risk profile against risk appetite limits e.g. foreign exposure and risk limits, liquidity and solvency ratios which are contained in the market risk framework incorporating market and country risk policies approved by the board.

(ii) *Exposure to Interest Rate Risk*

in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps.

(e) Operational Risk

The Operational risk is a risk of losses resulting from inadequate or failed internal processes, people, and systems or from external events.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. The responsibility is supported by the development of overall Bank standards for the management of operational risks. Compliance with these standards is supported by a programme of periodic reviews undertaken by internal audit. The results of internal audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the Board Risk Committee and senior management of the Bank.

Risk measurement and control

Interest rate, credit, liquidity, operational risk and other risks are actively managed by independent risk control groups to ensure compliance with the Bank's risk policy. The Bank's risk exposure limits are assessed regularly to ensure their appropriateness given the Bank's objectives and strategies and current market conditions.

(5) PROPERTY AND EQUIPMENT

(a) INVESTMENT PROPERTY

The Bank has classified some of its Properties according to IAS 40 –Investment Properties. The standard recognizes properties which are solely held for rental purposes or capital appreciation in the long term or both. For mixed use property, those partly occupied by the owner and partly rented out, the percentage of occupation determines its classification as per the IAS 40.10. If the percentage is significant then it falls under Plant, Properties and Equipment (PPE) but where insignificant it falls under Investment Properties.

Though the standard is silent on definition of significant, the assumption of materiality will guide while determining the threshold. Anything greater than 10% will greatly influence the decision maker. In the case of the Bank, the percentage of usage for Karura Training centre, Upper Hill properties and Dandora Plot is insignificant, hence classified under Investment Properties contrary to owner occupation at Postbank House Nairobi (49%); Postbank Mombasa (25%); Postbank Nakuru (50%); and Postbank Eldoret (100%) which is significant, and falls under Plant Property and Equipment (PPE).

Equally the International Accounting Standard (IAS 16) – considers Plant, Properties and Equipment (PPE) as tangible assets held for use in production or supply of goods or services, for rentals to others, or for administrative purposes and are expected to be used for more than one period. The standard also allows a choice of accounting model to use either cost model or revaluation model. In our case we opted for revaluation model.

(b) REVALUATION AND COST MODEL

The Bank has used the Revaluation and depreciating model for Land and Buildings while for all other classes of assets, Cost and depreciating model has been applied as per IAS 16.

(c) PROPERTY AND EQUIPMENT AND DEPRECIATION

Leasehold properties for which the lease has 99 years or more to run are stated at cost or

valuation and are not depreciated. Other assets are stated and depreciated at cost.

Depreciation is calculated on a straight-line basis, at rates estimated to write off the assets over

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

their expected useful lives.

The following depreciation rates are used:

| Category | Rate p.a. |
|---------------------------------|-----------|
| Buildings | 2.5 % |
| Show stands | 20.0 % |
| Motor vehicles | 25.0 % |
| Furniture and fittings | 12.5 % |
| Electronic office equipment | 20.0 % |
| Non-electronic office equipment | 12.5 % |
| Computer hardware | 20.0 % |
| Computer software | 20.0 % |

(d) INTANGIBLE ASSETS

Software licence costs and computer software that is not an integral part of the related hardware are initially recognised at cost, and subsequently carried at cost less accumulated amortisation and accumulated impairment losses. Costs that are directly attributable to the production of identifiable computers software products controlled by the bank are recognised as intangible assets. Amortisation is calculated using the straight line method to write down the cost of each licence or item of software to its residual value over its estimated useful life using annual rate of 20%.

(6) STOCKS

Stocks comprise of stationery and drugs in the staff clinic which are valued at cost.

(7) CASH AND CASH EQUIVALENTS

Cash and cash equivalents for the purposes of the cash flow statement comprise cash and bank balances net of bank overdraft, deposits in commercial banks and financial institutions and Treasury bills, treasury and corporate bonds as at the balance sheet date.

(8) FOREIGN CURRENCY TRANSACTIONS

On initial recognition, all transactions are recorded in the functional currency (the currency of the primary economic environment in which the bank operates), which is Kenya Shillings.

Foreign currency transactions during the year are converted into Kenya shilling equivalent at rates ruling at the transaction date. Assets and liabilities at the statement of financial position date which are expressed in foreign currency are translated into Kenya shillings at the rates ruling at the transaction date. The resulting differences from conversion and translation are dealt with in the profit and loss account in the year in which they arise.

(9) EMPLOYMENT BENEFIT

(a) POST-EMPLOYMENT BENEFIT OBLIGATIONS

The bank operates a retirement benefits plan for its employees, the assets of which are held in a separate trustee administered scheme managed by a Fund Manager. The contributions made by the Bank both to the Defined Benefit and Defined Contribution retirement scheme and to the Provident Fund are charged to the profit and loss account in the year of contribution.

From year 2011, the Bank and the employees also contribute to the National Social Security Fund (NSSF), a national defined contribution scheme. Contributions are determined by local

statute and the company's contributions are charged to the profit and loss account in the year to which they relate. Before year 2011, the Bank and employees were not making any

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

contribution to the National Social Security Fund (NSSF). This resulted to a penalty, hence a liability to the Bank of Kshs. 297,490,025, payable in three years from August 2014. The amount has since been fully paid as at 31st December 2017.

(b) SHORT TERM EMPLOYEE BENEFITS

The estimated monetary liability for employees' accrued annual leave entitlement at the balance sheet date is recognised as an employment cost accrual.

(10) PROVISION FOR DOUBTFUL DEBTS

Provision is made on debtors that are considered to be doubtful. Bad debts are written off when all reasonable steps to recover them have been taken without success.

(11) REVALUATION RESERVE

The revaluation reserve relates to property and equipment. The reserve is non-distributable. Revaluation reserves are made up of periodic adjustments arising from fair valuations of Property and equipment. Movement in the revaluation reserve are shown in the statement of changes in equity Kshs **2,388,250,796**

(12) REVENUE RESERVE

This represents undistributed profits/accumulated losses from current and previous years including prior year adjustments. The accumulated loss as at 31st December 2017 is Kshs - **11,020,457,848**.

(13) CONTINGENT LIABILITIES

Litigation is a common occurrence in the banking industry due to the nature of the business. Although there may be no assurance, the Directors believe based on the information available and advice from the legal experts that the claims will be defended successfully and therefore no provision has been made in the financial statement. The significant claims are described below:

- (i) Adella Kavisa & 73 others -vs-PostBank: Kshs. 166,084,453/= pension claim from retirees. It is not expected to be finalized next year.
- (ii) PostBank - vs - Simiyu Wasike: The land in dispute involves Postbank and Simiyu Wasike. It is in Upper Hill. The value of the property was Kshs. 319,200,000 in the year 2011.
- (iii) Other staff suits against the Bank sums to Kshs 19,928,087.00

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER
2017**

(14) INTEREST INCOME

| | 2017 | 2016 |
|----------------------------------|---------------------------|---------------------------|
| | Kshs | Kshs |
| Interest on Treasury Bills/Bonds | 622,718,851 | 554,273,675 |
| Interest on Term Deposits | 3,482,652 | 2,953,142 |
| Interest on Staff Loans | 44,664,770 | 110,972,806 |
| Interest on Visa Balances | <u>3,083,357</u> | <u>4,398,566</u> |
| | <u>673,949,630</u> | <u>672,598,189</u> |

(15) INTEREST EXPENSE

| | 2017 | 2016 |
|------------------------------|---------------------------|---------------------------|
| | Kshs | Kshs |
| Interest on:- | | |
| Bidii Savings Account | 207,069,667 | 211,578,174 |
| Step Account | 15,374,354 | 14,887,493 |
| Pension Account | 87,364,077 | 70,807,037 |
| Premium Savings Account | 235,063 | 69,549 |
| Premium Plus Account | 231,211,152 | 236,862,994 |
| Fixed Deposit Account | 1,951,218 | 1,959,934 |
| Save As You Earn Account | 5,091,946 | 9,406,518 |
| Staff Salary Account | 1,233,880 | 1,338,149 |
| Salary Account | 5,112,185 | 4,899,417 |
| Postbank Junior Account | 83,424 | 6,668 |
| Pamoja Account | 1,746,619 | 1,585,224 |
| Bidii Junior Trustee Account | 155,267 | 157,544 |
| Smata Youth Save | 3,799,970 | 3,922,745 |
| Waridi Account | 7,055,150 | 5,123,765 |
| M-Chama Account | 408,093 | 132,139 |
| Mobile Savings Account | 24,215 | 13,544 |
| Akiba Account | <u>39,125</u> | <u>37,650</u> |
| | <u>567,955,405</u> | <u>562,788,544</u> |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(16) FEES & COMMISSIONS INCOME

| | 2017 | 2016 |
|--|---------------------------|---------------------------|
| | Kshs | Kshs |
| Inactivity Fees | 14,267,290 | 74,764,358 |
| Salary Crediting Fees | 14,225,491 | 15,437,631 |
| Premature withdrawal Fees | 28,052,993 | 26,532,786 |
| Withdrawal Fees | 55,820,960 | 46,090,955 |
| Visa Fees | 6,185,624 | 6,167,413 |
| Card Fees | 24,043,428 | 59,716,930 |
| Western Union - MTS Commission | 54,330,818 | 50,070,658 |
| Citibank Commission | 541,140 | 1,209,457 |
| Pension commission | 69,203,500 | 69,475,590 |
| Money Transfer Commission (Others) | 25,218,989 | 31,818,887 |
| ATM withdrawal Fees | 46,492,904 | 48,497,684 |
| Bills Commission-Water & Electricity | 29,174,386 | 36,031,838 |
| AAR Loan Commission | 49,788,303 | 36,341,171 |
| Encashment Fee | 0 | 2,103,909 |
| Miscellaneous Fees & Commission (others) | <u>15,942,217</u> | <u>7,982,701</u> |
| | <u>433,288,043</u> | <u>512,241,968</u> |

(17) FEES AND COMMISSIONS EXPENSE

| | 2017 | 2016 |
|--|--------------------------|--------------------------|
| | Kshs | Kshs |
| Shared Costs Adjustments | 7,329,482 | 2,907,401 |
| Commission Expense-Money gram | 4,524,564 | 2,839,101 |
| Premium Paid Commission on Purchase of T/Bonds | 446,232 | 555,009 |
| Commission-Independent Agent | 80,044 | 140,355 |
| Mobile banking Expenses | 0 | 4,755,144 |
| Commission paid on deposit mobilisation | 9,978,186 | 8,808,757 |
| | <u>22,358,508</u> | <u>20,005,767</u> |

(18) FOREIGN EXCHANGE INCOME

| | 2017 | 2016 |
|--|--------------------------|--------------------------|
| | Kshs | Kshs |
| Forex gain on WU-MTS Transactions/Forex sale | 65,975,184 | 51,669,786 |
| Forex gain on MoneyGram Transactions | <u>19,004,379</u> | <u>25,005,772</u> |
| | <u>84,979,563</u> | <u>76,675,558</u> |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(19)(a) OTHER OPERATING INCOME

| | 2017 | 2016 |
|--|---------------------------|---------------------------|
| | Kshs | Kshs |
| Rental Income | 86,557,526 | 81,136,604 |
| Dividend income | 23,940 | 52,155 |
| Interest on bank accounts | 740,884 | 13,658 |
| Tender fees | 243,200 | 30,300 |
| Development Levy | 309,000 | - |
| Appreciation/Diminution in value of quoted investments | 431,600 | - 267,100 |
| Gain/(Loss) on sale of Property & equipment | 0 | -242,768 |
| Mobile Banking Fee | 9,031,992 | 10,133,377 |
| Capital Gain on Sale of Investments | 8,831,448 | - |
| Commission Income on Foreign Visa | 415,250 | 3,174,963 |
| Sundry income | <u>14,994,038</u> | <u>25,711,490</u> |
| | <u>121,578,878</u> | <u>119,742,679</u> |

Disclosure note

| | 2017 | 2016 |
|--|--------------------------|--------------------------|
| | Kshs | Kshs |
| 19.b Extra Ordinary Income | | |
| Receipt from Ailing Institutions | 62,076,491 | 10,975,743 |
| The Extra Ordinary Income is made up of the following: | | |
| Receipt from Ailing Institution – Trust Bank | 17,778,929 | 9,889,533 |
| Receipt from Ailing Institution – Postbank Credit Ltd | <u>44,297,562</u> | <u>1,086,210</u> |
| Total | <u>62,076,491</u> | <u>10,975,743</u> |

19.c Extra Ordinary Income

| | 2017 | 2016 |
|-----------------------|-------------|-------------|
| | Kshs | Kshs |
| Service Charge Income | 17,768,751 | *16,938,272 |

*Restated balance

(20) IMPAIRMENT LOSS ON DEPOSITS, LOANS AND ADVANCES

| | 2017 | 2016 |
|--|--------------------------|--------------------------|
| | Kshs | Kshs |
| Customers deposit | 5,416,667 | 15,000,000 |
| Visa card debtors | 5,416,667 | 3,000,000 |
| General Provisions-Including Staff loans | <u>2,166,666</u> | <u>2,000,000</u> |
| | <u>13,000,000</u> | <u>20,000,000</u> |

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER
2017**

(21) EMPLOYEE EXPENSES

| | 2017 | 2016 |
|------------------------------------|-----------------------------|-----------------------------|
| | Kshs | Kshs |
| Salaries and Wages | 787,776,065 | 764,478,508 |
| Pensions and Provident Fund contr. | 93,519,776 | 92,337,581 |
| Medical expenses | 55,720,405 | 66,083,983 |
| Staff training | 9,165,292 | 6,122,334 |
| Other staff expenses | <u>246,541,120</u> | <u>223,404,256</u> |
| | <u>1,192,722,658</u> | <u>1,152,426,662</u> |

(22) BOARD EXPENSES

| | 2017 | 2016 |
|--------------------------------|-------------------------|-------------------------|
| | Kshs | Kshs |
| Directors Honoraria | 80,000 | 960,000 |
| Directors Allowances | 1,189,325 | 7,926,311 |
| Directors Allowances Telephone | <u>44,360</u> | <u>50,700</u> |
| | <u>1,313,685</u> | <u>8,937,011</u> |

(23) OPERATING EXPENSES

| | 2017 | 2016 |
|---------------------------------|---------------------------|---------------------------|
| | Kshs | Kshs |
| Security expenses | 103,285,416 | 96,637,243 |
| Insurances | 15,156,163 | 13,279,175 |
| Office rent | 118,673,066 | 116,468,285 |
| Land rent and rates | 433,165 | 4,497,453 |
| Repairs and maintenance | 52,051,801 | 66,840,695 |
| Service charge | 9,681,612 | 9,328,829 |
| Agency fees – MTS | 21,071,140 | 13,561,058 |
| Licences | 89,158,042 | 66,449,358 |
| Grounds maintenance | 1,273,010 | 1,084,159 |
| Agency Expansion Project (WSBI) | 293,027 | <u>430,240</u> |
| | <u>411,076,442</u> | <u>388,576,495</u> |

(24) AMORTISATION FOR BONDS TRADING COST

| | 2017 | 2016 |
|-------------------|-------------|-------------|
| Amortisation Cost | 22,122,908 | 34,692,599 |

The amount of Kshs 22,122,908 relates to Treasury Bonds Premiums amortised monthly from 1.1.2017 to 31.12.2017

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER
2017**

(25) OTHER EXPENSES

| | 2017 | 2016 |
|-------------------------------------|---------------------------|---------------------------|
| | Kshs | Kshs |
| Travel and Subsistence allowances | 19,544,241 | 14,848,844 |
| Printing and stationery | 7,551,323 | 6,802,667 |
| Debt collection | 100,680 | 634,160 |
| Postage & telephone | 92,500,906 | 88,602,874 |
| Computer expenses | 10,944,629 | 8,309,892 |
| Motor Vehicle Expenses | 3,450,194 | 3,110,451 |
| Audit fees | 4,500,000 | 3,791,667 |
| Donations and subscriptions | 5,362,858 | 5,940,142 |
| Legal and professional fees | 18,012,582 | 13,294,062 |
| Electricity and water | 31,471,096 | 31,463,833 |
| Cleaning, Sanitation & Messengerial | 22,262,450 | 16,568,029 |
| Special Projects Launching | 4,199,601 | 1,659,100 |
| Newspapers and Periodicals | 728,286 | 566,752 |
| Transportation Costs | 0 | 20,000 |
| Procurement Costs | 638,719 | 1,046,060 |
| Excise Duty | 14,322,019 | 16,827,585 |
| Financial expenses | 5,811,854 | 8,945,158 |
| Selling & Marketing expenses | 65,058,138 | 96,570,029 |
| Operating Stationery | 2,998,391 | 3,415,013 |
| ATM processing charges | 0 | 1,447,020 |
| Hire of Motor Vehicles | 8,301,352 | 8,366,457 |
| ATM Card Cost | 10,120,151 | 17,406,318 |
| Research & Development | 0 | 354,000 |
| Miscellaneous expenses | <u>7,090,752</u> | <u>3,417,654</u> |
| | <u>334,970,222</u> | <u>353,407,767</u> |

(26) PROFIT (LOSS) FOR THE YEAR

| | Notes | 2017 | 2016 |
|--|--------------|-------------|-------------|
| | | Kshs | Kshs |
| The profit (loss) for the year is stated after charging: | | | |
| Directors emoluments | 22 | 1,313,685 | 8,937,011 |
| Audit fees | 25 | 4,500,000 | 3,791,667 |
| Depreciation/amortization intangible asset expense | 36a/37 | 113,228,671 | 127,445,528 |
| Bonds amortisation cost | 24 | 22,122,908 | 34,692,599 |
| Pension scheme contribution | 21 | 93,519,776 | 92,337,581 |
| and after crediting: - | | | |
| Dividends | 19a | 23,940 | 52,155 |
| Appreciation /Diminution in value of quoted investment | 33 | 431,600 | (267,100) |

Note. The Audit fees is based on budgeted amount during the year.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(27) EXPLANATION OF MATERIAL VARIANCE ON THE STATEMENT OF COMPARISON OF BUDGET AND ACTUAL FOR THE TWELVE MONTHS ENDING 31 DECEMBER 2017

INCOME

| | ACTUAL | BUDGET | VARIANCE | VARIANCE |
|--------------------------------|-------------|---------------|--------------|----------|
| a) Fees and commissions income | 433,288,043 | 820,819,581 | -387,531,538 | -47 |
| b) Other operating income | 121,578,878 | 160,210,602 | -38,631,724 | -24 |
| c) Operating income | 723,482,201 | 1,077,793,198 | -354,310,997 | -33 |

Non achievement of target

DIRECT EXPENSES

| | ACTUAL | BUDGET | VARIANCE | VARIANCE |
|---------------------------------|-------------|-------------|-------------|----------|
| d) Fees and commissions expense | 22,358,508 | 36,341,923 | 13,983,416 | -38 |
| e) Interest expense | 567,955,405 | 700,000,000 | 132,044,595 | -19 |

Non achievement of target leading to low spending

RECURRENT EXPENSES

| | ACTUAL | BUDGET | VARIANCE | VARIANCE |
|--|------------|-------------|------------|----------|
| f) Depreciation expenses | 94,601,599 | 132,064,200 | 37,462,601 | -28 |
| g) Amortisation cost-Intangible Assets | 18,627,072 | 30,446,283 | 11,819,210 | -39 |
| h) Board expenses. | 1,313,685 | 5,944,000 | 4,630,315 | -78 |

Non achievement of target and lower purchase of assets than anticipated.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(28) CASH AND CASH EQUIVALENTS

| | 2017 | 2016 |
|--------------|---------------------------|---------------------------|
| | Kshs | Kshs |
| Cash on Hand | 320,262,698 | 331,554,969 |
| Cash at Bank | <u>306,044,767</u> | <u>240,207,370</u> |
| | <u>626,307,465</u> | <u>571,762,339</u> |

The bulk of the cash at bank was held at Kenya Commercial Bank of Kenya and National Bank of Kenya who are the Bank's main bankers.

(29) FUNDS ON CALL AND SHORT NOTICE

| | 2017 | 2016 |
|--------------------------------|--------------------------|--------------------------|
| | Kshs | Kshs |
| Commercial Bank of Africa | 14,066,155 | 13,407,044 |
| Citibank | 10,900,000 | 10,000,000 |
| National Bank of Kenya | 10,004,193 | 9,632,298 |
| Kenya Commercial Bank of Kenya | 609,504 | <u>568,775</u> |
| | <u>35,579,852</u> | <u>33,608,117</u> |

The Bank has placed some of its funds in call accounts with commercial banks as listed above. For the year under review, the funds were invested at the following interest rates;

| BANK | RATE |
|---------------------------|-------------|
| Commercial Bank of Africa | 7.00% |
| Citibank | 7.00% |
| National Bank of Kenya | 7.00% |
| Kenya Commercial Bank(K) | 7.00% |

(30) INVESTMENT IN TREASURY BILLS & BONDS /OTHERS

| | 2017 | 2016 |
|------------------------------------|-----------------------------|-----------------------------|
| | Kshs | Kshs |
| Treasury Bonds-Available For Sale | 1,556,185,550 | 1,495,230,050 |
| Kengen Infrastructure Bond | 119,425,000 | 179,137,500 |
| Jamii Bora Bond | 20,000,000 | 20,000,000 |
| Funds under management (STANLIB) | 0 | 25,740,169 |
| Government of Kenya Treasury Bonds | <u>3,077,431,500</u> | <u>3,128,742,500</u> |
| | <u>4,773,042,050</u> | <u>4,848,850,219</u> |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

30(a) Investment in Treasury Bills and Bonds /Others

| ASSET | BALANCE ON 01.01.2017 | ADDITIONS IN THE YEAR 2017 | INCREASE/ DECREASE REVALUATION ADJUSTMENT IN YEAR 2017 |
|---|--------------------------|-------------------------------|---|
| | In Kshs | In Kshs | In Kshs |
| KENGEN Infrastructure Bond | 179,137,500 | | |
| Jamii Bora Bond | 20,000,000 | | |
| Funds Under Management (STANLIB) | 25,740,169 | | |
| GOK Treasury Bonds-Held to maturity | 3,128,742,500 | | |
| GOK Treasury Bonds-Available for sales | 1,495,230,050 | 694,385,082 | 38,212,926 |
| Total | 4,848,850,219 | 694,385,082 | 38,212,926 |

30(b) Change in Fair Value for Bonds AFS

| BALANCE ON 01.01.2017 | CAPITAL GAINS TRANSFER | REVALUATION INCREASE |
|-----------------------|------------------------|----------------------|
| In Kshs | In Kshs | In Kshs |
| 27,098,028 | -16,284,258 | 38,212,926 |

Note.

The effective weighted average rate of interest in respect to the above investments in year 2017 was:

| | |
|--|---------|
| KENGEN Infrastructure Bond | -12.50% |
| Jamii Bora Bond | -13.30% |
| Government of Kenya Treasury Bonds-HTM | -12.65% |
| Government of Kenya Treasury Bonds-AFS | -12.92% |

(31) INVESTMENT PROPERTY

| | 2017 Kshs | 2016 Kshs |
|---------------------|--------------|--------------|
| Investment property | 896,790,225 | 896,790,225 |

Included in the investment Property is-

- (i) Upper Hill Property whose market value is Ksh.319,200,000 but carried at book value of Ksh 27,390,225. Title to the Upper Hill property is in dispute with the current occupant of the premises claiming allottees interest absolutely. The matter is in court and the Bank expects a favourable outcome since it has a vesting right in the property and is holding it with an intention of selling or reinvesting.

The property is a piece of land with a building taken over from Thabiti Finance Ltd in lieu of deposits held for the Bank.

- (ii) Karura Training & Sports Complex valued at Ksh 864,400,000 as per the latest valuation

report undertaken by Transcountry Valuers Limited in October 2013.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(iii) Dandora Plot with a value of Ksh 5,000,000.

The reclassification of Dandora Plot and Karura Training centre from Property and Equipment to Investment property has been done as per IAS 40.

(32) STOCKS & DRUGS

| | 2017 | 2016 |
|------------|--------------------------|--------------------------|
| | Kshs | Kshs |
| Stationery | 11,964,229 | 16,698,046 |
| Drugs | <u>1,028,852</u> | <u>100,818</u> |
| | <u>12,993,081</u> | <u>16,798,864</u> |

(33) OTHER INVESTMENTS

| | 2017 | 2016 |
|--|-------------------------|-------------------------|
| | Kshs | Kshs |
| Quoted investments (cost) | 2,055,637 | 2,055,637 |
| Unquoted investment | <u>13,540,000</u> | <u>13,540,000</u> |
| | 15,595,637 | 15,595,637 |
| Less: Provision for diminution in market value of quoted /unquoted investments | <u>11,471,637</u> | <u>11,903,236</u> |
| | <u>4,124,001</u> | <u>3,692,401</u> |

Note.

- (i) Quoted investments were valued at Kshs.2,770,000 (2016 Kshs.2,338,400) using the Nairobi Securities Exchange market price at the close of the year realizing a gain of ksh431,600.

Quoted investments comprise of equity holdings in the following listed companies:

| Company | No. of Shares | Market price | Value 31.12.2017 | Value 31.12.2016 |
|--------------------|---------------|--------------|---------------------|---------------------|
| Kakuzi Ltd | 6500 | 329.00 | 2,138,500.00 | 1,826,500.00 |
| Total Kenya Ltd | 15000 | 23.50 | 352,500.00 | 267,000.00 |
| Bamburi Cement Ltd | 1550 | 180.00 | <u>279,000.00</u> | 244,900.00 |
| | | | 2,770,000.00 | 2,338,400.00 |

- (ii) Unquoted investment represents 80% of deposits in City Finance Bank (Jamii Bora Bank) converted into shares following their restructuring in year 2000.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(34) ACCOUNTS RECEIVABLES

| | Notes | 2017 Kshs | 2016 Kshs |
|---|-------|-----------------------------|-----------------------------|
| Postal Corporation of Kenya-Excess Deposits | | 780,394,108 | 780,399,108 |
| GOK-(KP&TC) | (i) | 405,231,629 | 405,231,629 |
| Commission Receivable from GoK | | 40,853,890 | 63,447,990 |
| Prepaid GoK Pension – PCK Payroll | | 512,767,484 | 456,675,801 |
| GoK Pension Cheques Receivable – PCK (ii) | | 268,553,158 | 268,553,158 |
| PCK Overdrawn Claimable | | 47,643,590 | 50,430,637 |
| Restitution (PCK) | | 58,847,809 | 56,911,716 |
| Directors Loans | | 3,327,044 | 3,327,044 |
| Staff loans | | 847,777,925 | 923,995,293 |
| Staff debtors – Personal Development Loan | | 138,267,614 | 150,876,889 |
| Interest Receivable -PDL | | 106,157,285 | 106,157,285 |
| Rent Receivables | | 60,203,935 | 50,618,767 |
| Staff Imprest | | 3,975,485 | 1,200,860 |
| Trade Debtors | (iii) | 126,700,382 | 219,927,482 |
| | | 3,400,701,338 | 3,537,753,659 |
| Provision for bad and doubtful debts: | | | |
| Trade Debtors | | -677,623,725 | -664,623,725 |
| | | <u>2,723,077,613</u> | <u>2,873,129,934</u> |

- (i) The Kshs. 405,231,629 relates to amount owing from the defunct KP&TC and has been outstanding since year 2005. The Government of Kenya has since given assurance of settlement of the amount, in effect through PCK.
- (ii) The amount of Kshs.268,553,158 relates to amount owed to Postbank by PCK in respect to pension's cheques and warrants handled by PCK on an agency agreement. This amount has been outstanding since year 2007 and the two organizations have made commitments to offset these amounts in the next financial year.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017
AGEING ANALYSIS RECEIVABLES

| 2017 | TOTAL | 0 to 30 Days | 31 to 60 Days | 61 to 90 Days | 91 and over Days |
|--------------------------------|----------------------|----------------------|----------------------|----------------------|-------------------------|
| PCK EXCESS DEPOSITS | 780,394,108 | - | - | - | 780,394,108 |
| KPTC - EXCESS DEPOSITS | 405,231,629 | - | - | - | 405,231,629 |
| PCK PREPAID GOK PENSION | 512,767,484 | (7,883,972) | 8,937,684 | 8,981,577 | 502,732,195 |
| PCK OVERDRAWN CLAIMABLE | 47,643,590 | - | - | (107,445) | 47,751,035 |
| STAFF DEBTORS PDL | 138,267,614 | 113,170,569 | | | 25,097,045 |
| INTERST RECEIVABLE PDL | 106,157,285 | (8,609,455) | 4,216,212 | (34,028,974) | 144,579,502 |
| DIRECTOR LOAN | 3,327,044 | - | - | - | 3,327,044 |
| STAFF LOANS | 847,777,925 | 749,961,279 | | | 97,816,646 |
| STAFF IMPREST | 3,975,485 | 13627 | (150,000) | (2,623,623) | 6,735,480 |
| COMMISSION RECEIVABLE -GOK | 40,853,890 | 5,688,000 | 5,612,400 | 5,601,900 | 23,951,590 |
| RESTITUTION -PCK | 58,847,809 | - | 28,500 | 1,000 | 58,818,309 |
| RENT RECEIVABLE | 60,203,935 | 20,949,885 | (2,357,353) | 68,373 | 41,543,030 |
| GOK PENSION CHEQUES RECEIVABLE | 268,553,158 | - | - | - | 268,553,158 |
| TRADE DEBTORS | 126,700,382 | 176,841,318 | 25,843,086 | 17,832,791 | (93,816,814) |
| TOTAL RECEIVABLES | 3,400,701,338 | 1,050,131,251 | 42,130,529 | (4,274,400) | 2,312,713,958 |
| PROVISION FOR BAD DEBTS | (677,623,725) | (2,000,000) | (1,000,000) | - | (674,623,725) |
| NET RECEIVABLES | 2,723,077,613 | 1,048,131,251 | 41,130,529 | (4,274,400) | 1,638,090,233 |

AGEING ANALYSIS RECEIVABLES

| 2016 | TOTAL | 0 to 30 Days | 31 to 60 Days | 61 to 90 Days | 91 and over Days |
|--------------------------------|----------------------|----------------------|----------------------|----------------------|-------------------------|
| PCK EXCESS DEPOSITS | 780,399,108 | - | - | - | 780,399,108 |
| KPTC - EXCESS DEPOSITS | 405,231,629 | - | - | - | 405,231,629 |
| PCK PREPAID GOK PENSION | 456,675,801 | 347,139,017 | (27,823,823) | 8,904,312 | 128,456,296 |
| PCK OVERDRAWN CLAIMABLE | 50,430,636 | - | 9,703 | 40 | 50,420,893 |
| STAFF DEBTORS PDL | 150,876,889 | (5,806,225) | (181,000) | (188,973) | 157,053,087 |
| INTERST RECEIVABLE PDL | 106,157,285 | 4,548,617.80 | 4,453,460.04 | 4,506,833.39 | 92,648,373.82 |
| DIRECTOR LOAN | 3,327,044 | - | - | - | 3,327,044 |
| STAFF LOANS | 923,995,293 | 843,908,237 | | | 80,087,056 |
| STAFF IMPREST | 1,200,860 | (1,803,375) | - | - | 3,004,235 |
| COMMISSION RECEIVABLE - GOK | 63,447,990 | 6,110,800 | 5,733,600 | 5,733,600 | 45,869,990 |
| RESTITUTION -PCK | 56,911,716 | - | - | - | 56,911,716 |
| RENT RECEIVABLE | 50,618,766 | 8,255,413 | (8,336,453) | (12,197,841) | 62,897,647 |
| GOK PENSION CHEQUES RECEIVABLE | 268,553,158 | - | - | - | 268,553,158 |
| TRADE DEBTORS | 219,927,482 | 6,616,559 | (4,848,488) | 11,801,598 | 206,357,813 |
| TOTAL RECEIVABLES | 3,537,753,659 | 1,208,969,044 | (30,993,001) | 18,559,570 | 3,275,460,121 |
| PROVISION FOR BAD DEBTS | (664,623,725) | (1,666,667) | (1,666,667) | (1,666,667) | (659,623,725) |

| | | | | | |
|-----------------|---------------|---------------|--------------|------------|---------------|
| NET RECEIVABLES | 2,873,129,934 | 1,207,302,378 | (32,659,667) | 16,892,903 | 2,615,836,397 |
|-----------------|---------------|---------------|--------------|------------|---------------|

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(35) PREPAYMENTS AND OTHER ASSETS

| | Note | 2017 Kshs | 2016 Kshs |
|---|------|-----------------------------|-----------------------------|
| Accrued interest on Treasury Bonds | | 83,608,741 | 95,510,898 |
| Discount on Treasury Bonds | | 47,738,766 | 41,025,070 |
| Fixed deposits in ailing financial institutions | | 417,007,051 | 479,083,542 |
| Transitorial Accounts - Postbank (i) | | 1,078,181,457 | 1,277,890,113 |
| Premium on Treasury Bonds (Prepaid) | | 307,015,011 | 329,137,919 |
| Other Assets and Prepayments | | <u>917,928,138</u> | <u>877,801,249</u> |
| | | 2,851,479,164 | 3,100,448,791 |
| Provision for bad and doubtful debts: | | | |
| Amounts due from subsidiary and deposits | | <u>-417,007,051</u> | <u>-479,083,542</u> |
| | | <u>2,434,472,113</u> | <u>2,621,365,250</u> |

(i) The amount of Kshs. 1,078,181,457 under Transitorial accounts relates to balances held in accounts used by the Bank to process internal payments. Therefore, the balance is not a realisable asset.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017
36. (a) PROPERTY AND EQUIPMENT - 2017

| | LAND | BUILDING | LEASEHOLD | MOTOR VEHICLES | FURNITURE & FITTINGS | ELECTRONIC OFFICE EQPMT | NON ELECTRONIC OFFICE EQPMT | COMPUTER HARDWARE | FIXED ASSET CLEARING ACCOUNT | CAPITAL WORK IN PROGRESS | TOTAL |
|-----------------------|--------------------|--------------------|-----------|----------------|----------------------|-------------------------|-----------------------------|-------------------|------------------------------|--------------------------|----------------------|
| Cost or Valuation | | | | | | | | | | | |
| At 1 Jan. 2017 | 854,500,000 | 1,053,550,000 | 6,500,000 | 29,123,656 | 314,420,670 | 242,119,643 | 73,823,634 | 616,360,976 | (18,682,089) | 4,170,684 | 3,175,887,174 |
| ADDITIONS | 0 | 0 | 0 | 0 | 4,651,708 | 3,623,930 | 726,423 | 6,199,275 | 403,376 | 5,778,438 | 21,383,150 |
| CAPITALISED | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | | 0 | 0 |
| WORKS | | | | | | | | | | | |
| DISPOSAL A/C | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | | 0 | 0 |
| DISPOSALS ADJ | 0 | 0 | 0 | 0 | | | | | | | |
| COST 31.12.2017 | 854,500,000 | 1,053,550,000 | 6,500,000 | 29,123,656 | 319,072,378 | 245,743,573 | 74,550,057 | 622,560,251 | -18,278,713 | 9,949,122 | 3,197,270,324 |
| DEPRECIATION | | | | | | | | | | | |
| DEPRE.01.01.17 | 0 | 306,280,583 | 6,500,000 | 29,816,600 | 238,417,368 | 196,434,301 | 63,503,382 | 547,411,263 | | 0 | 1,388,363,497 |
| CHARGED 2017 | 0 | 26,338,750 | | (692,944) | 15,770,707 | 13,861,289 | 2,510,514 | 36,120,339 | | 0 | 94,601,599 |
| WRITE BACK | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | | 0 | -692,944 |
| DISPOSALS | 0 | 0 | 0 | 0 | | | | | | 0 | 0 |
| DEPRE.31.12.17 | - | 332,619,333 | 6,500,000 | 29,123,656 | 254,188,074 | 210,295,590 | 66,013,896 | 583,531,602 | - | - | 1,482,272,152 |
| NBV 31.12.2017 | 854,500,000 | 720,930,667 | 0 | 0 | 64,884,303 | 35,447,983 | 8,536,161 | 39,028,647 | -18,278,713 | 9,949,122 | 1,714,998,172 |
| NBV 31.12.2016 | 854,500,000 | 747,269,417 | 0 | * -692,944 | 76,003,303 | 45,685,342 | 10,320,252 | 68,949,712 | -18,682,089 | 4,170,684 | 1,787,523,677 |

*Overstated accumulated depreciation charged in year 2016 was adjusted during the financial period.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

36. (b) PROPERTY AND EQUIPMENT - 2016

| Cost or Valuation | LAND | BUILDING | LEASEHOLD | MOTOR VEHICLES | FURNITURE & FITTINGS | ELECTRONIC OFFICE EQPMT | NON ELECTRONIC OFFICE EQPMT | COMPUTER HARDWARE | FIXED ASSET CLEARING ACCOUNT | CAPITAL WORK IN PROGRESS | TOTAL |
|-----------------------|--------------------|--------------------|-----------|-----------------|----------------------|-------------------------|-----------------------------|-------------------|------------------------------|--------------------------|----------------------|
| At 1 Jan. 2016 | 854,500,000 | 1,053,550,000 | 6,500,000 | 29,123,656 | 318,969,756 | 230,660,330 | 77,446,759 | 607,588,811 | (25,209,638) | 2,520,082 | 3,155,649,756 |
| ADDITIONS | 0 | 0 | 0 | 0 | 2,298,807 | 12,976,338 | 501,752 | 25,572,532 | 6,527,549 | 1,650,602 | 49,527,580 |
| CAPITALISED WORKS | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| DISPOSAL A/C | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| DISPOSALS ADJ | 0 | 0 | 0 | 0 | (6,847,892) | (1,517,025) | (4,124,877) | (16,800,367) | 0 | 0 | (29,290,161) |
| COST 31.12.2016 | 854,500,000 | 1,053,550,000 | 6,500,000 | 29,123,656 | 314,420,671 | 242,119,643 | 73,823,634 | 616,360,976 | (18,682,089) | 4,170,684 | 3,175,887,175 |
| DEPRECIATION | | | | | | | | | | | |
| DEPRE.01.01.16 | 0 | 279,941,833 | 6,500,000 | 27,741,950 | 226,906,081 | 178,654,571 | 64,787,736 | 523,783,363 | 0 | 0 | 1,308,315,534 |
| CHARGED 2016 | 0 | 26,338,750 | - | 2,074,651 | 18,359,178 | 19,296,755 | 2,840,523 | 40,428,268 | 0 | 0 | 109,338,125 |
| WRITE BACK | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| DISPOSALS | 0 | 0 | 0 | 0 | (6,847,892) | (1,517,025) | (4,124,877) | (16,800,367) | 0 | 0 | (29,290,161) |
| DEPRE.31.12.16 | 0 | 306,280,583 | 6,500,000 | 29,816,600 | 238,417,367 | 196,434,301 | 63,503,382 | 547,411,263 | 0 | 0 | 1,388,363,496 |
| NBV 31.12.2016 | 854,500,000 | 747,269,417 | 0 | -692,944 | 76,003,303 | 45,685,342 | 10,320,252 | 68,949,712 | (18,682,089) | 4,170,684 | 1,787,523,677 |
| NBV 31.12.2015 | 854,500,000 | 773,608,167 | - | 1,381,707 | 92,063,674 | 52,005,759 | 12,659,023 | 83,805,448 | (25,209,638) | 2,520,082 | 1,847,334,222 |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

36. (c) LAND AND BUILDINGS

| COST OR VALUATION | Land Kshs | Buildings Kshs | Show Stand Kshs | 2017 Total Kshs | 2016 Total Kshs |
|----------------------|---------------------------|-----------------------------|-------------------------|-----------------------------|-----------------------------|
| Long-term leasehold | 732,000,000 | 977,750,000 | - | 1,709,750,000 | 1,709,750,000 |
| Short-term leasehold | <u>122,500,000</u> | <u>75,800,000</u> | <u>6,500,000</u> | <u>204,800,000</u> | <u>204,800,000</u> |
| | <u>854,500,000</u> | <u>1,053,550,000</u> | <u>6,500,000</u> | <u>1,914,550,000</u> | <u>1,914,550,000</u> |

Included in short-term leasehold land and buildings is a property purchased in Mombasa. It was valued at Kshs.198.30 million subject to extension of lease period by another 45 years from the current 10 years. Initiative towards extension of the lease is in progress.

The figures used in the fixed assets schedule relate to 2013 valuation report carried out by Trans country Valuers Limited and approved by the Board in October 2013.

37. INTANGIBLE ASSETS

| | 2017 Kshs | 2016 Kshs |
|---------------------------|--------------------------|--------------------------|
| Cost | | |
| At 1 January | 575,214,934 | 514,034,535 |
| Additions | - | 61,180,400 |
| At 31 December | 575,214,934 | 575,214,935 |
| Amortisation | | |
| At 1 January | 490,442,331 | 472,334,928 |
| Amortization for the year | 18,627,072 | 18,107,403 |
| At 31 December | 509,069,403 | 490,442,331 |
| Carrying Amount | | |
| At 31 December | <u>66,145,531</u> | <u>84,772,604</u> |

The intangible assets are in respect of Internet and mobile banking software

(38) CUSTOMERS' SAVINGS AND DEPOSIT ACCOUNTS

| | 2017 | 2016 |
|----------------------------|------------------------------|------------------------------|
| | Kshs | Kshs |
| Bidii Savings Account | 8,422,775,102 | 8,217,019,123 |
| Junior Trust Account | 0 | 9,937,631 |
| STEP Account | 757,813,023 | 715,707,653 |
| Pension accounts (BSG) | 3,792,199,582 | 3,197,666,008 |
| Premium Savings Scheme | (21,862) | 6,865,356 |
| Premium Plus Account | 3,588,810,377 | 3,658,036,444 |
| Fixed Deposit Account | 75,065,185 | 83,833,838 |
| Save-As-You-Earn | 763,892,792 | 717,151,012 |
| Staff Salary Account | 67,993,050 | 75,731,287 |
| Salary Account | 247,692,300 | 230,136,497 |
| Postbank Junior Account | 15,348,381 | 7,687,403 |
| Corporate Clients | 432,712,820 | 432,018,719 |
| Smata Youth Save Account | 233,821,809 | 212,831,033 |
| Pamoja Chama Account | 81,642,950 | 71,812,219 |
| Mzalendo Account | 151,817 | 107,897 |
| Waridi Account | 382,068,647 | 276,787,964 |
| Independent Agent Accounts | 10,411,354 | 21,447,577 |
| M-chama Savings Account | 24,973,084 | 6,857,357 |
| M-sawa Savings Account | 1,742,512 | 1,207,100 |
| Akiba Saving Account | 2,009,852 | 1,822,735 |
| | <u>18,901,102,775</u> | <u>17,944,664,853</u> |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(39) ACCOUNTS PAYABLES AND ACCRUALS

| | Notes | 2017 Kshs | 2016 Kshs |
|---|-------|-----------------------------|-----------------------------|
| Trade creditors | | 59,374,467 | 42,536,218 |
| PCK Services rendered- GoK Pension/others | (i) | 534,372,812 | 533,056,749 |
| PCK Encashed Warrants Payable | (ii) | 462,078,751 | 462,078,751 |
| PCK- Pension Warrants | (iii) | 170,953,266 | 170,953,266 |
| GoK Pension Payroll | (iv) | 904,080,077 | 848,668,153 |
| Accrued Expenses | | 370,493,868 | 194,371,584 |
| NSSF Liability | | 0 | 52,060,754 |
| Other creditors | | 529,728,633 | 477,056,706 |
| | | <u>3,031,081,874</u> | <u>2,780,782,181</u> |

(i) PCK Services rendered- GOK Pension/others refers to amount payable to Postal Corporation of Kenya for services offered to our pensioners/regular customers for normal banking services.

(ii) PCK Encashed warrant payable refers to amount claimable by Postal Corporation of Kenya on disbursement of pension to pensioners.

The amount of Kshs.462,078,751 which has been outstanding since year 2007 will be settled along with expected amounts from PCK .

(iii) PCK -GoK Warrant is the un-accounted amount to pensioners account held by PCK. The amount of Kshs.170,953,266 which has been outstanding since year 2007 will be settled along with expected amounts from PCK.

(iv) GoK Pension Payroll is the un-applied amount to pensioners account held by PCK.

AGEING ANALYSIS OF ACCOUNTS PAYABLES AND ACCRUALS

| 2017 | TOTALS | 0 to 30 | 31 to 60 | 61 to 90 | 91 to 120 |
|---|-----------------------------|---------------------------|----------------------------|---------------------------|-----------------------------|
| Trade creditors | 59,374,467 | - | 33,521,834 | -13,157,503 | 39,010,136 |
| PCK Services rendered- GoK Pension/others (i) | 534,372,812 | - | - | 258,336 | 534,114,476 |
| PCK Encashed Warrants Payable (ii) | 462,078,751 | - | - | - | 462,078,751 |
| PCK- Pension Warrants (iii) | 170,953,266 | - | - | - | 170,953,266 |
| GoK Pension Payroll (iv) | 904,080,078 | -24,685,837 | -391,700 | -7,883,972 | 937,041,587 |
| Accrued Expenses | 370,493,868 | 19,532,954 | 154,905,337 | 5,290,880 | 190,764,697 |
| Other creditors | 529,728,632 | -13,870,814 | -344,791,302 | -2,800,151 | 891,190,899 |
| TOTALS | <u>3,031,081,874</u> | <u>-19,023,697</u> | <u>-156,755,831</u> | <u>-18,292,410</u> | <u>3,225,153,812</u> |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(40) GOK PENSION RESERVE FUND

| | 2017 | 2016 |
|--------|----------------------------|---------------------------|
| | Kshs | Kshs |
| Amount | <u>(74,381,227)</u> | <u>183,942,031</u> |

These are receipts from the Government of Kenya for payment of pension to senior citizen. The arrangement is that the Bank Pays pensioners on due date.

In year 2017 GoK owed the Bank Kshs74,381,227 being disbursement in excess of funds received. The status changed to payable in 2016 where bank owed GoK.Ksh.183,942,042 being unpaid fund.

(41) CAPITAL GRANTS

Capital grants were given to the Bank to support the following projects:

| | 2017 | 2016 |
|---|--------------------------|--------------------------|
| | Kshs | Kshs |
| Western Union Product | 2,013,211 | 2,013,211 |
| Bidii Product | 3,706,728 | 3,706,728 |
| Visa EMV Project | 229,458 | 229,458 |
| Smata, Mchama & Agency Expansion Projects | <u>6,957,640</u> | <u>6,957,640</u> |
| | <u>12,907,037</u> | <u>12,907,037</u> |

(42) CASH AND CASH EQUIVALENTS

| | 2017 | 2016 |
|--|-----------------------------|-----------------------------|
| | Kshs | Kshs |
| Bank and cash balances | 626,307,465 | 571,762,339 |
| Deposits in banks and Financial Institutions | 35,579,852 | 33,608,117 |
| Treasury Bills and Bonds | <u>4,773,042,050</u> | <u>4,848,850,219</u> |
| | <u>5,434,929,367</u> | <u>5,454,220,675</u> |

(43) RELATED PARTY TRANSACTIONS

The Banks main related parties are the Board members, key management personnel and staff. The following transactions were carried out with related parties.

| | 2017 | 2016 |
|----------------------------------|---------------------------|-----------------------------|
| | Kshs | Kshs |
| (i) Directors remuneration | | |
| Directors Honoraria | 80,000 | 960,000 |
| Directors Allowances | <u>1,233,685</u> | <u>7,926,311</u> |
| | <u>1,313,685</u> | <u>8,886,311</u> |
| (ii) Key management remuneration | | |
| Salaries and wages | 7,574,038 | 8,309,063 |
| (iii) Loans to staff | | |
| Welfare loans | 847,777,925 | 923,995,293 |
| Personal development Loan | <u>138,267,614</u> | <u>150,876,889</u> |
| | <u>986,045,539</u> | <u>1,074,872,182</u> |

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

Interest income on these loans was Kshs 44,664,770 (2016 - 110,972,806). The effective interest rate for welfare loans is 5% while for personal development loan is 14%. Staff mortgages and car loans are secured by charging the related property to the Bank.

(iv) Loans to Directors

No loan was issued to directors in the year under review. However, outstanding loan balance of Kshs 3,327,044 relates to loans advanced to former directors.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(44) LIQUIDITY RISK

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period as at 31 December 2017 to the contractual maturity date.

| A. Assets | Matured | Matured in less than a month | 1 months less than 3 months | 3 months less than 6 months | 6 months less than 1 year | 1 year less than 3 years | 3 years less than 5 years | over 5 years | Totals |
|---------------------------------------|----------------------|------------------------------|-----------------------------|-----------------------------|---------------------------|--------------------------|---------------------------|-----------------------|-----------------------|
| Bank and Cash Balances | 626,307,465 | - | - | - | - | - | - | - | 626,307,465 |
| Investment in T/bills + Bonds | - | 235,733,034 | 453,213,229 | 516,586,940 | 253,146,940 | 652,133,264 | 1,213,565,112 | 1,448,663,531 | 4,773,042,050 |
| Funds on call and short notice | - | 35,579,852 | - | - | - | - | - | - | 35,579,852 |
| Investment Property | - | - | - | - | - | - | - | 896,790,225 | 896,790,225 |
| Other Investment | - | - | 4,124,001 | - | - | - | - | - | 4,124,001 |
| Other Assets | 552,595,029 | 1,068,287,703 | 735,322,723 | 779,050,447 | 649,095,120 | 662,722,349 | 723,469,436 | - | 5,170,542,807 |
| Gok Pension Reserve Fund Account | 74,381,227 | - | - | - | - | - | - | - | 74,381,227 |
| Property and Equipment | - | - | 20,881,322 | - | 30,766,963 | 31,234,547 | 250,150,411 | 1,381,964,929 | 1,714,998,172 |
| Intangible Assets | - | - | 18,142,044 | 26,600,079 | 21,403,408 | - | - | - | 66,145,531 |
| Total Assets | 1,253,283,721 | 1,339,600,589 | 1,231,683,319 | 1,322,237,466 | 954,412,431 | 1,346,090,160 | 2,187,184,959 | 3,727,418,685 | 13,361,911,330 |
| B. Liabilities and Reserves | | | | | | | | | |
| Other Liabilities | 100,572,776 | 473,701,859 | 436,123,256 | 574,045,299 | 417,300,671 | 375,067,768 | 654,270,245 | - | 3,031,081,874 |
| Customers' Savings & Deposit accounts | 1,305,052,455 | 1,719,829,244 | 1,802,132,879 | 2,026,611,924 | 1,959,511,623 | 2,004,367,826 | 2,287,411,603 | 5,796,185,221 | 18,901,102,775 |
| Capital Grants | - | - | - | - | - | - | - | 12,907,037 | 12,907,037 |
| Revaluation Reserves | - | - | - | - | - | - | - | 2,388,250,796 | 2,388,250,796 |
| Change un Fair value for Bonds | - | 27,098,028 | 21,928,668 | - | - | - | - | - | 49,026,696 |
| Revenue Reserves | - | - | - | - | - | - | - | -11,020,457,848 | -11,020,457,848 |
| Total Liabilities and Reserves | 1,405,625,231 | 2,220,629,131 | 2,260,184,803 | 2,600,657,223 | 2,376,812,294 | 2,379,435,594 | 2,941,681,848 | -2,823,114,794 | 13,361,911,330 |
| A 0 B Liquidity GAP | -152,341,510 | -881,028,542 | -1,028,501,484 | -1,278,419,757 | -1,422,399,863 | -1,033,345,434 | -754,496,889 | 6,550,533,479 | - |

Customers' Savings and deposits accounts relate to Savings and fixed account balances. Although classified under this band, previous experience has shown these to be stable and of long term in nature.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2017

(45) CONSOLIDATION

Consolidated Accounts are not prepared as the Bank's wholly owned subsidiary, Postbank Credit Limited, is under liquidation.

(46) TAXATION

Kenya Post Office Savings Bank is exempt from Corporation Tax under Income Tax Act Cap 470 of the laws of Kenya.

(47) COMPARATIVES

Where necessary, comparative figures have been adjusted to conform to reporting under IFRS.

(48) EMPLOYEES

The average number of employees during the year was 720 (2015-763).

(49) SUBSEQUENT EVENTS

There have been no events subsequent to the financial year end with significant impact on the financial statements for the year ended December 31, 2017

(50) NETWORK OF POSTBANK BRANCHES

The total number of branches during the year was 99.

NETWORK OF POSTBANK BRANCHES

HEAD OFFICE

Postbank House
Banda Street
P.O. Box 30311 – 00100
Tel: (020) 2229551-6 Ext. 155 Fax 341557
NAIROBI

NAIROBI NORTH REGION

Eastleigh Branch:
P.O. Box 30313 - 00100
Tel: (020) 6761892 Fax 6761892
NAIROBI

Kikuyu Branch:
P.O. Box 30311 - 00100
Tel: (066) 31630 Fax 31630
KIKUYU

Ruiru Branch:
P.O. Box 190
Tel: (067) 54320 Fax 55441
RUIRU

Karuri Branch
P.O. Box 30311 – 00100
Tel: (066) 51683 Fax 51685
NAIROBI

KARIOBANGI
P.O. Box 30313 – 00100
Tel: (020) 2229551-6 341557

NAIROBI SOUTH REGION

Afya Centre Branch:
Tom Mboya Street
P.O. Box 30311 - 00100
Tel: (020)2 229551-6 Ext. 322, 340-2, 330-1
NAIROBI

Karen Branch:
P.O. Box 30313 - 00100
Tel: (020) 884547 Fax 884548
NAIROBI

Viwandani Sub Branch:
P.O. Box 30311 - 00100
Tel: (020) 2229551-6 Fax 553356
NAIROBI

Wote - Makueni Branch:
P.O. Box 944
Tel: (044) 33371, Fax 33388
MAKUENI
P.O. Box 944

Emali
P.O. Box 30313-00100
Tel: (020) 2445490
NAIROBI

Garissa Branch:
P.O. Box 745
Tel: (046) 2169 Fax 3194
GARISSA

Limuru Branch:
P.O. Box 170
Tel: (066) 71293 Fax 72278
LIMURU

Uthiru Branch:
P.O. Box 30313 - 00100
Tel: (020) 631927 Fax 631927
NAIROBI

Matuu Branch
P.O. Box 30311 - 00100
Tel: (067) 4355282 Fax 4355283
NAIROBI

Cannon House Branch:
Parliament Road
P.O. Box 30311 - 00100
Tel: (020) 2229551-6 Ext. 239, 319
NAIROBI

Kitui Branch:
P.O. Box 668
Tel: (044) 22993 Fax 23046
KITUI

Kangundo Branch:
P.O. Box 30311
Tel: (044) 621150, Fax 621148
KANGUNDO

Ngong Branch:
P.O. Box 30311 – 00100
Tel: (045) 41047 Fax 41048
NAIROBI

Mlolongo
P.O. Box 30313 – 0100
Tel: (045) 2445491
NAIROBI

Githurai Branch:
P.O. Box 30311- 00100
Tel: (020) 811032 Fax 811032
NAIROBI

Mwingi Branch:
P.O. Box 510
Tel: (044) 22308 Fax 22308
MWINGI

Westland Branch:
P.O. Box 30313-00100
Tel: (020) 4440581, 4450965
NAIROBI

Uchumi Ngong Road Branch
P.O. Box 30311 – 00100
Tel: (020) 2229551-6
NAIROBI

Enterprise Road Branch:
P.O. Box 30311 - 00100
Tel: (020) 2229551-6 Ext. 270
NAIROBI

Kajiado
P.O. Box 30313-00100
Tel: (020) 2455105
NAIROBI

Ongata Rongai Branch
P.O. Box 30311 – 00100
Tel: (045) 24178 Fax 24179
NAIROBI

Kawagware Branch
P.O. Box 30313 - 0100
Tel: (045) 2445491
NAIROBI

Kiambu Branch:
P.O. Box 145
Tel: (066) 22913 Fax 22914
KIAMBU

Ngara Branch:
P.O. Box 30313 - 00100
Tel: (020) 3744837 Fax 3744837
NAIROBI

Thika Branch:
P.O. Box 1819
Tel: (020) 31193 Fax 30076
THIKA

Customer Service Centre
P.O. Box 30311 – 00100
Tel: (020) 2229551-6 Fax 210593
NAIROBI

Kitengela Branch:
P.O. Box 30311 - 00100
Tel: (045) 22526 Fax 22518
NAIROBI

Kibwezi Branch
P.O. Box 30311 - 00100
Tel: (044) 3500422 Fax 3500432
NAIROBI

NETWORK OF POSTBANK BRANCHES (continued)

MT. KENYA REGION

Chuka Branch:
P.O. Box 616
Tel: (064) 630443 Fax 630064
CHUKA

Embu Branch:
P.O. Box 1245
Tel: (068) 30740 Fax 30727
EMBU

Karatina Branch:
P.O. Box 246
Tel: (061) 72537 Fax 72977
NYERI

Kerugoya Branch:
P.O. Box 1020
Tel: (060) 21893 Fax 21833
KERUGOYA

Meru Branch:
P.O. Box 3270
Tel: (064) 30381 Fax 32573
MERU

Murang'a Sub- Branch:
P.O. Box 122
Tel: (060) 31083 Fax 31038
MURANG'A

Nanyuki Branch:
P.O. Box 416
Tel: (062) 32210 Fax 32820
NANYUKI

Nyeri Branch:
P.O. Box 246
Tel: (061) 2034348 Fax 2032189
NYERI

Waruguru Branch
P.O. Box 1245
Tel: (060) 48236 Fax 48081
EMBU

Maua Branch
P.O. Box 767
Tel: (064) 21150
MAUA

Isiolo Branch
P.O. Box 696
Tel: (064) 52355
ISILOLO

Marsabit Branch
P.O. Box 75925
MARSABIT

COAST REGION

Chaani Branch:
P.O. Box 90563
Tel: (041) 3434077 Fax 3433485
MOMBASA

Likoni Branch:
P.O. Box 90563
Tel: (041) 2451070 Fax 2451017
MOMBASA

Kilifi Branch:
P.O. Box 90563
Tel: (041) 522399 Fax 522399
MOMBASA

Malindi Branch:
P.O. Box 5196
Tel: (042) 30599 Fax 20512
MALINDI

Moi Avenue, Mombasa, Branch:
P.O. Box 90563
Tel: (041) 2230969, Fax 2230945
MOMBASA

Mtwapa Branch:
P.O. Box 90563
Tel: (041) 5486939 Fax 5486470
MOMBASA

Kisauni Branch:
P.O. Box 90563
Tel: (041) 474000 Fax 474333
MOMBASA

Mariakani Branch:
P.O. Box 90563
Tel: (041) 33425, Fax 33430
MOMBASA

Voi Branch:
P.O. Box 452
Tel: (043) 5352228 Tel: (043) 30253
Fax 30253
VOI

Savani House, Mombasa, Branch:
Digo Road
P.O. Box 90563
Tel: (041) 2314424
Fax 2223771
MOMBASA

Ukunda Branch:
P.O. Box 90563
Tel: (040) 3203248
Fax 3203248
MOMBASA

Taita Taveta
P.O. Box 90563
Tel: (040) 3203248
Fax: (043) 5352124
MOMBASA

Watamu
P. O. Box 90563
Tel: (041) 200115
MOMBASA

RIFT VALLEY REGION

Gilgil Branch:
P.O. Box 30313
Tel: (050) 4002143, Fax 4002144
GILGIL

Eldoret Branch:
P.O. Box 2270
Tel: (053) 2062295 Fax 2063025
ELDORET

Kabarnet Branch:
P.O. Box 442
Tel: (053) 22354 Fax 21130
KABARNET

Nyahururu Branch
P.O. Box 342
Tel: (065) 32251 Fax 32857
NYAHURURU

Kapsabet Branch:
P.O. Box 800
Tel: (053) 52535 Fax 62497
KAPSABET

Kitale Branch:
P.O. Box 821
Tel: (054) 30394 Fax 31297
KITALE

Molo Branch:
P.O. Box 4199
Tel: (051) 721561 Fax 721097
MOLO

Narok Branch:
P.O. Box 634
Tel: (050) 22030 Fax 222425
NAROK

Naivasha Branch
P.O. Box 675
Tel: (050) 2021335 Fax 2020200
NAIVASHA

Nakuru Branch:
P.O. Box 4199
Tel: (051) 2215710 Fax 2211400
NAKURU

Nandi Hills Branch:
P.O. Box 321
Tel: (053) 643146 Fax 643146
NANDI HILLS

Iten Branch
P.O. Box
Iten

Maralal Branch
P.O. Box
Maralal

Kapenguria
P.O. Box 614
Kapenguria

Lodwar
P.O. Box
Lodwar

Eldama Ravine Branch
P.O. Box
Eldama Ravine

NETWORK OF POSTBANK BRANCHES (continued)

WESTERN REGION

Bungoma Branch:

P.O. Box 944
Tel: (055) 30418 Fax 30318
BUNGOMA

Busia Branch:

P.O. Box 183
Tel: (055) 22278 Fax 22157
BUSIA

Homa Bay Branch:

P.O. Box 203
Tel: (054) 22388 Fax 21466
HOMA BAY

Kakamega Branch:

P.O. Box 2444
Tel: (056) 30630 Fax 31069
KAKAMEGA

Kisii Branch:

P.O. Box 740
Tel: (058) 30800 Fax 30341
KISII

Kisumu Branch:

P.O. Box 183
Tel: (057) 2023955 Fax 2021358
KISUMU

Mumias Branch:

P.O. Box 523
Tel: (056) 641410 Fax 641233
MUMIAS

Siaya Branch:

P.O. Box 203
Tel: (057) 321213 Fax 321213
SIAYA

Suna - Migori Branch:

P.O. Box 1059
Tel: (059) 20857 Fax 20034
MIGORI

Luanda Branch:

P.O. Box 859
Tel: (057) 351230 Fax 351232
LUANDA

Webuye Branch:

P.O. Box 1014
Tel: (055) 41027 Fax 41025
WEBUYE

Sare Awendo

P. O. Box 183
Tel: (059) 43417 Fax 43417
AWENDO

Keroka

P.O. Box 138
Tel: (058) 520037 Fax 520037
KEROKA

Bomet Branch:

P.O. Box 778
Tel: (051) 22439 Fax 22440
LITEIN

Kericho Branch:

P.O. Box 1031
Tel: (052) 30378 Fax 32115
KERICHO

Mbita Branch

P. O. Box
MBITA

Bondo Branch

P.O. Box 183
BONDO

Kehancha Branch

P.O. Box 207
Kehancha

Nyamira Branch

PO Box 364
Nyamira

Oyugis Branch

P.O Box 1986
Oyugis