

REPUBLIC OF KENYA



OFFICE OF THE AUDITOR-GENERAL

REPORT

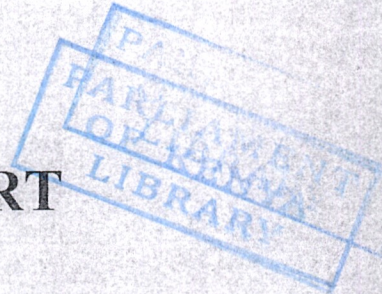
OF

THE AUDITOR-GENERAL

ON

THE FINANCIAL STATEMENTS OF  
CONSOLIDATED BANK OF KENYA LIMITED

FOR THE YEAR ENDED  
31 DECEMBER 2015



**CONSOLIDATED BANK OF KENYA LIMITED**

**ANNUAL REPORT AND  
FINANCIAL STATEMENTS**

**31 DECEMBER 2015**

CONSOLIDATED BANK OF KENYA LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2015

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# CONSOLIDATED BANK OF KENYA LIMITED

## CORPORATE INFORMATION

### DIRECTORS:

Dr. B. Ateng - Chairman  
T. Kiyai - Chief Executive Officer  
Cabinet Secretary, National Treasury  
Managing Trustee - NSSF  
M. Cherogony  
E. Vitisia  
C. Amira  
P. Muhindi  
Dr. R. Omollo  
J. Koskey

### AUDIT COMMITTEE:

J. Koskey-Chairman  
E. Vitisia  
C. Amira  
R. Omollo

### STAFF COMMITTEE:

C. Amira-Chairman  
T. Kiyai  
Cabinet Secretary, National Treasury  
Managing Trustee - NSSF

### COMPANY SECRETARY:

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

### AUDITORS:

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

Delegated auditors:  
Deloitte & Touche  
Certified Public Accountants (Kenya)  
Deloitte Place, Waiyaki Way, Muthangari  
P. O. Box 40092 – 00100, Nairobi

### LEGAL ADVISERS:

Hamilton Harrison & Mathews  
ICEA Building  
P.O. BOX 30333 - 00100 Nairobi, Kenya

### RISK COMMITTEE.

P. Muhindi-Chairman  
E. Vitisia  
M. Cherogony

### FINANCE AND CREDIT COMMITTEE:

M. Cherogony-Chairman  
E. Vitisia  
P. Muhindi  
T. Kiyai  
Managing Trustee - NSSF  
Cabinet Secretary - Treasury

### REGISTERED OFFICE:

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

### CORRESPONDENT BANKS:

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

Deutsche Bank AG London  
Winchester House  
1 Great Winchester Street  
London EC2N 2DB

### LEGAL ADVISERS :

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

## CONSOLIDATED BANK OF KENYA LIMITED

### STATEMENT OF CORPORATE GOVERNANCE

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

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

#### **Business ethics**

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

#### **Board of Directors**

The names of the Directors as at the date of this report are set out on page 2.

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

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

#### **a) Directors' Emoluments and Loans**

The remuneration of all directors is subject to the guidelines issued by the Office of the President on terms and conditions of service for State Corporations. The directors are not eligible for membership of the pension scheme and do not participate in any of the bank's bonus schemes. Information on the compensation received and the dealings of the directors with the bank are included in notes 11 and 37 to the financial statements.

#### **b) Related Party Transactions**

There have been no materially significant related party transactions, pecuniary transactions or relationships between the bank and its Directors or Management except those disclosed in Note 37 to the financial statements.

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

#### **Audit Committee**

The board is mandated to raise the standards of corporate governance by reviewing the quality and effectiveness of the internal control systems, the internal and external audit functions and the quality of financial reporting. In addition to advising the Board on best practice, the committee also monitors management's compliance with relevant legislation, regulations and guidelines as well as the bank's laid down policies and procedures. The committee has direct access to the Internal Audit function and the Company Secretary. During the year the committee received and reviewed the findings of the internal and external audit reports and management's action to address them.

## CONSOLIDATED BANK OF KENYA LIMITED

### STATEMENT OF CORPORATE GOVERNANCE (Continued)

#### **Risk Committee**

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

#### **Finance and Credit Committee**

The committee is mandated to review and make recommendations on the bank's credit, financial and accounting policies, and review and make recommendations on the bank's Annual Budget, oversight of the overall lending policy of the bank and deliberate and consider loan applications beyond the credit discretion limits set for management. The committee also reviews and considers all issues that may materially impact the present and future quality of the bank's credit risk management function as well as the quality of the loan portfolio and ensure adequate bad debt provisions are maintained in line with the Central Bank of Kenya prudential guidelines. The committee also reviews, approves and monitors the management's compliance with applicable statutory provisions, bank policies and guidelines relating to the monitoring of price, liquidity, exchange rate and interest rate risks.

#### **Staff Committee**

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

CONSOLIDATED BANK OF KENYA LIMITED

STATEMENT OF CORPORATE GOVERNANCE (Continued)

Board meeting attendance

During the year under review, the Board held main board meetings and working committee meetings. The Board members attendance for 2015 is as follows:

| Name  | Board Meeting               |                   |      | Audit Committee             |                   |      | Risk & Compliance Committee |                   |      | Credit & Finance Committee  |                   |      | Staff Committee             |                   |      |
|---|-----------------------------|-------------------|------|-----------------------------|-------------------|------|-----------------------------|-------------------|------|-----------------------------|-------------------|------|-----------------------------|-------------------|------|
|   | Meetings required to attend | Meetings attended | %    | Meetings required to attend | Meetings attended | %    | Meetings required to attend | Meetings attended | %    | Meetings required to attend | Meetings attended | %    | Meetings required to attend | Meetings attended | %    |
| T. Kiyai - (Chief Executive Officer)                            | 10                          | 10                | 100% | -                           | -                 | -    | 3                           | 3                 | 100% | 4                           | 3                 | 75%  | 1                           | 1                 | 100% |
| George Omamo - Representing Cabinet Secretary National Treasury | 17                          | 15                | 88%  | -                           | -                 | -    | -                           | -                 | -    | 8                           | 7                 | 88%  | 3                           | 3                 | 100% |
| Dr A Omerikwa - Managing Trustee - NSSF                         | 17                          | 4                 | 24%  | -                           | -                 | -    | -                           | -                 | -    | 8                           | 3                 | 38%  | 3                           | 1                 | 33%  |
| Dr Raymond Omollo*  | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    |
| Joseph Koskey**   | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    |
| Dr B Ateng - (Chairman)   | 17                          | 16                | 94%  | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    | -                           | -                 | -    |
| Amb C. Amira  | 17                          | 17                | 100% | 5                           | 5                 | 100% | -                           | -                 | -    | -                           | -                 | -    | 3                           | 3                 | 100% |
| M Cherogony   | 17                          | 13                | 77%  | 5                           | 5                 | 100% | 4                           | 4                 | 100% | 8                           | 6                 | 75%  | -                           | -                 | -    |
| P Muhirdi   | 17                          | 17                | 100% | -                           | -                 | -    | 4                           | 4                 | 100% | 8                           | 8                 | 100% | -                           | -                 | -    |
| E Vitiia  | 17                          | 17                | 100% | 5                           | 5                 | 100% | 4                           | 4                 | 100% | 8                           | 8                 | 100% | -                           | -                 | -    |

Dr. Raymond Omollo was appointed on 23 December 2015 hence he did not attend any board meeting.

\*\* Joseph Koskey was appointed on 26 February 2016 hence he did not attend any board meeting.

# CONSOLIDATED BANK OF KENYA LIMITED

## STATEMENT OF CORPORATE GOVERNANCE (Continued)

### Board performance evaluation

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

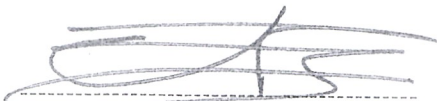
### Shareholders

The list of the shareholders and their individual holdings at the year ended 31 December 2015 was as follows:

|  | No. of<br>Ordinary<br>Shares | %            | No. of<br>Preference<br>Shares | %            |
|--|------------------------------|--------------|--------------------------------|--------------|
| Cabinet Secretary/The National Treasury  | 35,000,000                   | 77.9%        | -                              | -            |
| National Social Security Fund            | 2,225,000                    | 5.0%         | 8,050,000                      | 22.3%        |
| Kenya National Assurance (2001)          | 1,094,487                    | 2.4%         | 3,958,300                      | 11.0%        |
| Kenya National Assurance Company Limited | 835,513                      | 1.9%         | 3,021,700                      | 8.4%         |
| Kenya Pipeline Company Limited           | 720,000                      | 1.6%         | 2,631,500                      | 7.3%         |
| Kenya National Examination Council       | 695,000                      | 1.5%         | 2,520,000                      | 7.0%         |
| Public Trustees                          | 660,000                      | 1.5%         | 2,420,000                      | 6.7%         |
| Telkom Kenya Limited                     | 620,000                      | 1.4%         | 2,250,000                      | 6.2%         |
| National Hospital Insurance Fund         | 590,000                      | 1.3%         | 2,120,000                      | 5.9%         |
| LAPTRUST Retirement Services Limited     | 486,000                      | 1.1%         | 1,756,000                      | 4.9%         |
| <b>Total of 10 above</b>                 | <b>42,926,000</b>            | <b>95.6%</b> | <b>28,727,500</b>              | <b>79.7%</b> |
| <b>Other Shareholders</b>                | <b>1,994,000</b>             | <b>4.4%</b>  | <b>7,329,000</b>               | <b>20.3%</b> |
| <b>TOTAL SHAREHOLDING</b>                | <b>44,920,000</b>            | <b>100%</b>  | <b>36,056,500</b>              | <b>100%</b>  |

### Compliance

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



Director

29 March 2016

# CONSOLIDATED BANK OF KENYA LIMITED

## REPORT OF THE DIRECTORS

The directors have pleasure in presenting their report together with the audited financial statements of Consolidated Bank of Kenya limited (“the bank”) for the year ended 31 December 2015, which show the state of affairs of the bank.

### ACTIVITIES

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

| RESULTS  | Sh'000        |
|--|---------------|
| Profit before taxation                                 | 48,789        |
| Taxation charge  | (4,367)       |
|  | <hr/>         |
| Profit for the year transferred to accumulated deficit | <u>44,442</u> |

### DIVIDEND

The directors do not recommend the payment of a dividend for the year (2014: nil).

### DIRECTORS

The current members of the board of directors are shown on page 2. The following changes took place in the directorship during the year.

- Thomas Kiyai was appointed as Chief Executive Officer on 10 April 2015.
- Dr. Raymond Omollo was appointed as director on 23 December 2015.
- Joseph Kosgey was appointed as director on 26 February 2016.
- Bertha Dena resigned from the board with effect from 2 October 2015.
- Methuselah Rono's term as director ended on 11 March 2015.

### AUDITORS

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

Deloitte & Touche, who were nominated by the Auditor General, carried out the audit of the financial statements for the year ended 31 December 2015.

### BY ORDER OF THE BOARD

  
Secretary

Nairobi

29 March 2016

CONSOLIDATED BANK OF KENYA LIMITED

STATEMENT OF DIRECTORS' RESPONSIBILITIES

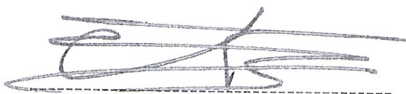
The Kenyan Companies Act requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the bank as at the end of the financial year and of its operating results for that year. It also requires the directors to ensure that the bank keeps proper accounting records which disclose with reasonable accuracy at any time the financial position of the bank. They are also responsible for safeguarding the assets of the bank.

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

The directors accept responsibility for the annual 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 and in the manner required by the Kenyan Companies Act. The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the bank and of its operating results. The directors further accept responsibility for the maintenance of accounting records which may be relied upon in the preparation of financial statements, as well as adequate systems of internal financial control.


The directors have considered the bank's non-compliance with the minimum capital requirements of the Central Bank of Kenya Prudential Guidelines as discussed in note 3 to the financial statements which indicates that, at 31 December 2015, the bank's total regulatory capital to risk weighted assets ratio was 9.4% which is below the CBK minimum prudential ratio of 14.5%. The directors are taking the necessary measures to ensure compliance. As a result, the National Treasury, as one of the principal shareholders, have so far injected Shs 500 million in additional capital to help reverse the situation. The bank is in the process of raising additional capital of Shs 1.8 billion through a rights issue which was approved by the shareholders during the Extra ordinary General Meeting held on 15 December 2015. The rights issue process is expected to be concluded on 4 April 2016.

Nothing else has come to the attention of the directors to indicate that the bank will not remain a going concern for at least the next twelve months from the date of this statement.



Director

29 March 2016



Director



## OFFICE OF THE AUDITOR-GENERAL

### REPORT OF THE AUDITOR-GENERAL ON CONSOLIDATED BANK OF KENYA LIMITED FOR THE YEAR ENDED 31 DECEMBER 2015

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#### REPORT ON THE FINANCIAL STATEMENTS

The accompanying financial statements of Consolidated Bank of Kenya Limited set out on pages 11 to 67, which comprise the statement of financial position as at 31 December 2015, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information have been audited on my behalf by Deloitte & Touche, auditors appointed under Section 39 of the Public Audit Act, 2003. The auditors have duly reported to me the results of their audit and on the basis of their report, I am satisfied that all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit were obtained.

#### **Management's Responsibility for the Financial Statements**

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

The Directors are also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 13 of the Public Audit Act, 2003.

#### **Auditor-General's Responsibility**

My responsibility is to express an opinion on these financial statements based on the audit and report in accordance with the provisions of Section 15(2) and (3) of the Public Audit Act, 2003 and submit the audit report in compliance with Article 229(7) of the Constitution of Kenya. The audit was conducted in accordance with International Standards on Auditing. Those standards require compliance with ethical requirements and that the audit be planned and performed to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation

and fair presentation of the financial statements 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **Opinion**

In my opinion, the financial statements present fairly, in all material respects, the financial position of Consolidated Bank of Kenya as at 31 December 2015, and of its profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and comply with the Kenyan Companies Act, Cap 486 of the Laws of Kenya, and the Banking Act.

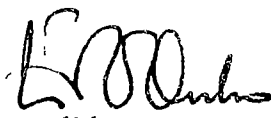
### **Emphasis of Matter**

I draw your attention to note 3 to these financial statements which indicates the bank had not been issued with a banking license for the year 2016 as a result of not having met the capital adequacy ratios as at 31 December 2015. The issuance of the license depends on conclusion of measures taken by directors to ensure compliance with the capital adequacy ratios. My opinion is not qualified in respect of this matter.

### **REPORT ON OTHER LEGAL REQUIREMENTS**

As required by the Kenyan Companies Act, I report based on the audit, that:

- i. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit;
- ii. in my opinion, proper books of account have been kept by the Bank, so far as appears from the examination of those books; and
- iii. the bank's statement of financial position and statement of profit or loss and other comprehensive income are in agreement with the books of account.



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

**Nairobi**

**07 June 2016**

CONSOLIDATED BANK OF KENYA LIMITED


STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME  
FOR THE YEAR ENDED 31 DECEMBER 2015


|  | Note  | 2015<br>Sh'000 | 2014<br>Sh'000 |
|--|-------|----------------|----------------|
| INTEREST INCOME  | 6     | 1,957,414      | 2,054,537      |
| INTEREST EXPENSE   | 7     | (938,585)      | (1,141,396)    |
| NET INTEREST INCOME  |       | 1,018,829      | 913,141        |
| Fee and commission income  | 8     | 316,865        | 321,886        |
| Foreign exchange trading income  | 9     | 36,628         | 43,796         |
| Other operating income   | 10    | 642,713        | 102,298        |
| OPERATING INCOME   |       | 2,015,035      | 1,381,121      |
| Operating expenses   | 11    | (1,377,562)    | (1,207,539)    |
| Impairment charge on loans and advances                                    | 19    | (588,684)      | (447,772)      |
| PROFIT/(LOSS) BEFORE TAXATION  |       | 48,789         | (274,190)      |
| TAXATION CHARGE  | 13(a) | (4,367)        | (7,442)        |
| PROFIT/(LOSS) FOR THE YEAR   |       | 44,422         | (281,632)      |
| OTHER COMPREHENSIVE INCOME   |       |                |                |
| <i>Items that may be reclassified subsequently to profit or loss:</i>      |       |                |                |
| Net fair value gains on available-for-sale financial assets                | 21    | 2,973          | 1,845          |
| <i>Items that will not be reclassified subsequently to profit or loss:</i> |       |                |                |
| Surplus on revaluation of property and equipment                           | 22    | -              | 151,293        |
| Deferred tax on revaluation  | 27    | -              | (45,388)       |
| Total other comprehensive income   |       | 2,973          | 107,750        |
| TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR                             |       | 47,395         | (173,882)      |
| EARNINGS/(LOSS) PER SHARE  |       | Sh             | Sh             |
| Basic and diluted  | 14    | 0.87           | (14.14)        |

CONSOLIDATED BANK OF KENYA LIMITED  
STATEMENT OF FINANCIAL POSITION  
AS AT 31 DECEMBER 2015

|   |       | 31 December<br>2015 | 31 December<br>2014 |
|---|-------|---------------------|---------------------|
| ASSETS  | Note  | Sh'000              | Sh'000              |
| Cash and balances with Central Bank of Kenya      | 15    | 759,717             | 1,406,318           |
| Balances due from banking institutions            | 16(a) | 104,709             | 162,098             |
| Government securities                             | 17    | 2,688,034           | 2,823,524           |
| Loans and receivables                             | 18    | 9,221,256           | 9,212,581           |
| Other assets                                      | 20    | 250,486             | 235,315             |
| Quoted equity shares                              | 21    | 6,879               | 3,906               |
| Taxation recoverable                              | 13(c) | 12,165              | 6,300               |
| Property and equipment                            | 22    | 844,438             | 937,706             |
| Intangible assets                                 | 23    | 240,695             | 281,984             |
| Prepaid operating lease rentals                   | 24    | 7,149               | 7,319               |
| <b>TOTAL ASSETS</b>                               |       | <b>14,135,528</b>   | <b>15,077,051</b>   |
| <b>LIABILITIES AND SHAREHOLDERS' FUNDS</b>        |       |                     |                     |
| <b>LIABILITIES</b>                                |       |                     |                     |
| Deposits and balances due to banking institutions | 16(b) | 275,463             | 533,502             |
| Customer deposits                                 | 25    | 9,996,058           | 10,641,959          |
| Other liabilities                                 | 26    | 240,821             | 238,875             |
| Deferred tax liability                            | 27    | 38,677              | 40,752              |
| Borrowings  | 28    | 1,969,294           | 2,054,143           |
| <b>TOTAL LIABILITIES</b>                          |       | <b>12,520,313</b>   | <b>13,509,231</b>   |
| <b>SHAREHOLDERS' FUNDS</b>                        |       |                     |                     |
| Share capital                                     | 29(b) | 1,619,530           | 1,119,530           |
| Capital awaiting allotment                        | 29(c) | -                   | 500,000             |
| Revaluation surplus                               | 30    | 396,372             | 405,999             |
| Accumulated deficit                               | 31    | (533,841)           | (531,528)           |
| Statutory reserve                                 | 32    | 127,143             | 70,781              |
| Fair value reserve                                | 33    | 6,011               | 3,038               |
| <b>TOTAL SHAREHOLDERS' FUNDS</b>                  |       | <b>1,615,215</b>    | <b>1,567,820</b>    |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS' FUNDS</b>  |       | <b>14,135,528</b>   | <b>15,077,051</b>   |

The financial statements on pages 11 to 67 were approved and authorised for issue by the Board of Directors on 29 March 2016 and were signed on its behalf by:

  
Director

  
Director

  
Chief Executive Officer

  
Company Secretary

CONSOLIDATED BANK OF KENYA LIMITED

STATEMENT OF CHANGES IN EQUITY  
FOR THE YEAR ENDED 31 DECEMBER 2015

|                                     | Note  | Capital awaiting allotment<br>Sh'000 | Share capital<br>Sh'000 | Revaluation surplus<br>Sh'000 | Accumulated deficit<br>Sh'000 | Statutory reserve<br>Sh'000 | Fair value reserve<br>Sh'000 | Total<br>Sh'000 |
|-------------------------------------|-------|--------------------------------------|-------------------------|-------------------------------|-------------------------------|-----------------------------|------------------------------|-----------------|
| At 1 January 2014                   |       | -                                    | 1,119,530               | 308,135                       | (276,143)                     | 88,987                      | 1,193                        | 1,241,702       |
| Loss for the year                   |       | -                                    | -                       | -                             | (281,632)                     | -                           | -                            | (281,632)       |
| Other comprehensive income          |       | -                                    | -                       | 105,905                       | -                             | -                           | 1,845                        | 107,750         |
| Total comprehensive loss            |       | -                                    | -                       | 105,905                       | (281,632)                     | -                           | 1,845                        | (173,882)       |
| Transfer of excess depreciation     | 30    | -                                    | -                       | (11,487)                      | 11,487                        | -                           | -                            | -               |
| Deferred tax on excess depreciation | 30    | -                                    | -                       | 3,446                         | (3,446)                       | -                           | -                            | -               |
| Transfer from statutory reserve     | 32    | -                                    | -                       | -                             | 18,206                        | (18,206)                    | -                            | -               |
| Capital awaiting allocation         | 29(c) | 500,000                              | -                       | -                             | -                             | -                           | -                            | 500,000         |
| At 31 December 2014                 |       | 500,000                              | 1,119,530               | 405,999                       | (531,528)                     | 70,781                      | 3,038                        | 1,567,820       |
| At 1 January 2015                   |       | 500,000                              | 1,119,530               | 405,999                       | (531,528)                     | 70,781                      | 3,038                        | 1,567,820       |
| Profit for the year                 |       | -                                    | -                       | -                             | 44,422                        | -                           | -                            | 44,422          |
| Other comprehensive income          |       | -                                    | -                       | -                             | -                             | -                           | 2,973                        | 2,973           |
| Total comprehensive income          |       | -                                    | -                       | -                             | 44,422                        | -                           | 2,973                        | 47,395          |
| Capital allotted in the year        | 29(c) | (500,000)                            | 500,000                 | -                             | -                             | -                           | -                            | -               |
| Transfer of excess depreciation     | 30    | -                                    | -                       | (13,753)                      | 13,753                        | -                           | -                            | -               |
| Deferred tax on excess depreciation | 30    | -                                    | -                       | 4,126                         | (4,126)                       | -                           | -                            | -               |
| Transfer to statutory reserve       | 32    | -                                    | -                       | -                             | (56,362)                      | 56,362                      | -                            | -               |
| At 31 December 2015                 |       | -                                    | 1,619,530               | 396,372                       | (533,841)                     | 127,143                     | 6,011                        | 1,615,215       |

CONSOLIDATED BANK OF KENYA LIMITED

STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED 31 DECEMBER 2015

|  | Note  | 2015<br>Sh'000 | 2014<br>Sh'000 |
|--|-------|----------------|----------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                          |       |                |                |
| Cash generated from operations                                       | 34(a) | 153,478        | 1,051,792      |
| Tax paid   | 13(c) | (12,307)       | -              |
| Net cash generated from operating activities                         |       | 141,171        | 1,051,792      |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                          |       |                |                |
| Acquisition of property and equipment                                | 22    | (11,331)       | (9,665)        |
| Acquisition of intangible assets                                     | 23    | (19,482)       | (27,976)       |
| Net cash used in investing activities                                |       | (30,813)       | (37,641)       |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                          |       |                |                |
| Proceeds from capital injection                                      | 29(c) | -              | 500,000        |
| Repayment of borrowings  | 28    | (330,878)      | (297,428)      |
| Net cash (used in)/generated from financing activities               |       | (330,878)      | 202,572        |
| NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS DURING THE YEAR |       | (220,520)      | 1,216,723      |
| CASH AND CASH EQUIVALENTS AT 1 JANUARY                               |       | 466,632        | (750,091)      |
| CASH AND CASH EQUIVALENTS AT 31 DECEMBER                             | 34(b) | 246,112        | 466,632        |

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS

### 1 REPORTING ENTITY

Consolidated Bank of Kenya Limited (The“bank”) provides commercial banking services. The bank is incorporated in Kenya under the Kenyan Companies Act and is domiciled in Kenya.

The address of its registered office is as follows:

Consolidated Bank House, Koinange Street

P O Box 51133

Nairobi- 00200

### 2 (a) ACCOUNTING POLICIES

#### Adoption of new and revised international financial reporting standards (IFRS's)

i) *New standards and amendments to published standards effective for the year ended 31 December 2015*

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

#### **IAS 19 Defined Benefit Plans: Employee Contributions**

The amendments to IAS 19 clarify the accounting treatment for contributions from employees or third parties to a defined benefit plan.

According to the amendments, discretionary contributions made by employees or third parties reduce service cost upon payment of these contributions to the plan. When the formal terms of the plan specify contributions from employees or third parties, the accounting depends on whether the contributions are linked to service, as follows:

- If the contributions are not linked to services (e.g. contributions are required to reduce a deficit arising from losses on plan assets or from actuarial losses), they affect the remeasurement of the net defined benefit liability (asset).
- If contributions are linked to services, they reduce service costs. If the amount of contribution is dependent on the number of years of service, the entity should reduce service cost by attributing it to the contributions to periods of service using the attribution method required by IAS 19 paragraph 70 (for the gross benefits). If the amount of contribution is independent of the number of years of service, the entity is permitted to either reduce service cost in the period in which the related service is rendered, or reduce service cost by attributing the contributions to the employees' periods of service in accordance with IAS 19 paragraph 70. The amendment requires retrospective application.

The directors of the Company do not anticipate that the application of the standard will have a significant impact on the group's financial statements since the group doesn't have a defined benefit plan.

#### **Annual Improvements 2010-2012 Cycle**

The Annual Improvements to IFRSs 2010-2012 Cycle include a number of amendments to various IFRSs, which are summarised below:

The amendment to IFRS 2 is to clarify the definition of vesting condition and market condition to ensure the consistent classification of conditions attached to a share-based payment. It also adds definitions for 'performance condition' and 'service condition' which were previously included as part of the definition of 'vesting condition'. The amendment requires prospective application.

The amendment to IFRS 3 clarifies that contingent consideration should be measured at fair value at each reporting date, irrespective of whether or not the contingent consideration falls within the scope of IFRS 9 or IAS 39. Changes in fair value (other than measurement period adjustments as defined in IFRS 3) should be recognised in profit and loss. The amendment to IFRS 3 requires prospective application.

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS

### 2 (a) ACCOUNTING POLICIES (Continued)

#### **Adoption of new and revised International Financial Reporting Standards (IFRS) (Continued)**

- i) *New standards and amendments to published standards effective for the year ended 31 December 2015 (Continued)*

##### **Annual Improvements 2010-2012 Cycle (Continued)**

The amendment to IFRS 8(i) requires an entity to disclose the judgements made by management in applying the aggregation criteria to operating segments, including a brief description of the operating segments aggregated and the economic indicators assessed in determining whether the operating segments share similar economic characteristics; and (ii) clarifies that a reconciliation of the total of the reportable segments' assets to the entity's assets should only be provided if information about the amount of segment assets are regularly provided to the chief operating decision-maker.

The amendment to IFRS 13 clarifies that the issuance of IFRS 13 and consequential amendments to IAS 39 and IFRS 9 did not remove the ability to measure short-term receivables and payables with no stated interest rate at their invoice amounts without discounting, if the effect of discounting is immaterial. This amendment does not include any effective date because this is just to clarify the intended meaning in the basis for conclusions.

The amendment to IAS 16 and IAS 38 remove perceived inconsistencies in the accounting for accumulated depreciation/amortisation when an item of property, plant and equipment or an intangible asset is revalued. The amended standards clarify that the gross carrying amount is adjusted in a manner consistent with the revaluation of the carrying amount of the asset and that accumulated depreciation/amortisation is the difference between the gross carrying amount and the carrying amount after taking into account accumulated impairment losses

The amendment to IAS 24 clarifies that a management entity providing key management personnel services to the reporting entity or to the parent of the reporting entity is a related party of the reporting entity. Consequently, the reporting entity should disclose as related party transactions the amounts incurred for the service paid or payable to the management entity for the provision of key management personnel services. However, disclosure of the components of compensation to key management personnel that is paid by the management entity to the management entity's employees or directors is not required

##### **Annual Improvements 2011-2013 Cycle**

The Annual Improvements to IFRSs 2011-2013 Cycle include a number of amendments to various IFRSs, which are summarised below:

The amendments to IFRS 3 clarify that the standard does not apply to the accounting for the formation of all types of joint arrangement in the financial statements of the joint arrangement itself.

The amendments to IFRS 13 clarify that the scope of the portfolio exception for measuring the fair value of a group of financial assets and financial liabilities on a net basis includes all contracts that are within the scope of, and accounted for in accordance with, IAS 39 or IFRS 9, even if those contracts do not meet the definitions of financial assets or financial liabilities within IAS 32

The amendments to IAS 40 clarify that IAS 40 and IFRS 3 are not mutually exclusive and application of both standards may be required. Consequently, an entity acquiring investment property must determine whether:

- (a) the property meets the definition of investment property in terms of IAS 40; and
- (b) the transaction meets the definition of a business combination under IFRS 3

The directors of the Company do not anticipate that the application of these amendments will have a significant impact on the group's financial statements

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS

### 2 (a) ACCOUNTING POLICIES (Continued)

#### Adoption of new and revised International Financial Reporting Standards (IFRS) (Continued)

ii) *Relevant new and amended standards and interpretations in issue but not yet effective in the year ended 31 December 2015*

| <i>New and Amendments to standards</i> | <i>Effective for annual periods beginning on or after</i> |
|--|---|
| IFRS 15                                | 1 January 2018  |
| Amendments to IAS 16 and IAS 38        | 1 January 2016  |
| IFRS 9                                 | 1 January 2018  |
| Amendments to IFRS 11                  | 1 January 2016  |

iii) *Impact of new and amended standards and interpretations on the financial statements for the year ended 31 December 2015 and future annual periods*

#### **IFRS 15 Revenue from Contracts with Customers**

In May 2015, IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related Interpretations when it becomes effective. The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

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

Under IFRS 15, an entity recognises revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15. The standard is not likely to have any material impact on the bank's financial statements.

#### **Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation**

The amendments to IAS 16 prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for amortisation of an intangible asset. This presumption can only be rebutted in the following two limited circumstances:

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

The amendments apply prospectively for annual periods beginning on or after 1 January 2016. Currently, the bank uses the reducing balance method for depreciation and amortisation for its property, and equipment, and intangible assets respectively. The amendments are not likely to have any material impact on the bank's financial statements.

CONSOLIDATED BANK OF KENYA LIMITED  
NOTES TO THE FINANCIAL STATEMENTS

2 (a) ACCOUNTING POLICIES (Continued)

**Adoption of new and revised International Financial Reporting Standards (IFRSs) (Continued)**

iii) *Impact of new and amended standards and interpretations on the financial statements for the year ended 31 December 2015 and future annual periods (Continued)*

**IFRS 9 Financial Instruments**

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

- All recognised financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement are required to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognised in profit or loss.
- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.
- The directors of the bank anticipate that the application of IFRS 9 in the future may have a significant impact on amounts reported in respect of the bank's financial assets and financial liabilities (e.g. the bank will classify financial assets as subsequently measured at either amortised cost or fair value). However, it is not practicable to provide a reasonable estimate of the effect of IFRS 9 until a detailed review has been completed.

**Annual Improvements 2012-2014 Cycle**

The amendments to IFRS 5 adds specific guidance in IFRS 5 for cases in which an entity reclassifies an asset from held for sale to held for distribution or vice versa and cases in which held-for-distribution accounting is discontinued

The amendments to IFRS 7 adds additional guidance to clarify whether a servicing contract is continuing involvement in a transferred asset for the purpose of determining the disclosures required. Clarifies the applicability of the amendments to IFRS 7 on offsetting disclosures to condensed interim financial statements.

The amendments to IAS 19 clarifies that the high quality corporate bonds used in estimating the discount rate for post-employment benefits should be denominated in the same currency as the benefits to be paid (thus, the depth of the market for high quality corporate bonds should be assessed at currency level)

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS

### 2 (a) ACCOUNTING POLICIES (Continued)

#### **Adoption of new and revised International Financial Reporting Standards (IFRS) (Continued)**

##### *iii) Impact of new and amended standards and interpretations on the financial statements for the year ended 31 December 2015 and future annual periods (Continued)*

The amendment to IAS 34 clarifies the meaning of 'elsewhere in the interim report' and requires a cross-reference

The directors of the Company do not anticipate that the application of these amendments will have a significant impact on the Company's financial statements.

#### **IFRS 11 Accounting for Acquisitions of Interests in Joint Operations**

The amendments to IFRS 11 provide guidance on how to account for the acquisition of an interest in a joint operation in which the activities constitute a business as defined in IFRS 3 Business Combinations. Specifically, the amendments state that the relevant principles on accounting for business combinations in IFRS 3 and other standards (e.g. IAS 12 Income Taxes regarding recognition of deferred taxes at the time of acquisition and IAS 36 Impairment of Assets regarding impairment testing of a cash-generating unit to which goodwill on acquisition of a joint operation has been allocated) should be applied. The same requirements should be applied to the formation of a joint operation if and only if an existing business is contributed to the joint operation by one of the parties that participate in the joint operation. A joint operator is also required to disclose the relevant information required by IFRS 3 and other standards for business combinations.

Entities should apply the amendments prospectively to acquisitions of interests in joint operations (in which the activities of the joint operations constitute businesses as defined in IFRS 3) occurring from the beginning of annual periods beginning on or after 1 January 2016

The directors of the Company do not anticipate that the application of the standard will have a significant impact on the Company's financial statements

##### *iv) Early adoption of standards*

The bank did not early adopt new or amended standards in 2015

#### **Statement of compliance**

The financial statements have been prepared in accordance with International Financial Reporting Standards. Additional information required by regulatory bodies is included where appropriate.

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

#### **Basis of preparation**

The financial statements have been prepared on the historical cost basis of accounting except for certain properties that are measured at revalued amounts and certain financial instruments, measured at fair value:

#### **Consolidation**

The financial statements of the dormant subsidiaries listed in note 35 have not been consolidated as the amounts involved are not material and would, therefore, be of no real value.

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 2 (a) ACCOUNTING POLICIES (Continued)

#### **Investments in subsidiary companies**

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

#### **Interest income and expense**

Interest income and expense for all interest bearing financial instruments are recognised in the profit or loss on accrual basis using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. 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 when appropriate, a shorter period) to the net carrying amount of the financial asset or liability.

The calculation of the effective interest rate includes all fees and commissions 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.

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

#### **Fees and commission income**

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

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

Other fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

#### **Property and equipment**

Property and equipment are stated at cost or as professionally re-valued from time to time less accumulated depreciation and any accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. The bank's policy is to professionally revalue property at least once every three years

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

#### **Depreciation**

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

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 2 (a) ACCOUNTING POLICIES (Continued)

##### Depreciation (Continued)

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

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

The depreciation rates on fixtures, fittings, equipment & ATMs was changed during the year from the previous useful life of 8 years to 5 years.

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

##### Intangible assets - computer software costs

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

The amortisation of intangible assets was changed during the year from the previous useful life of 10 years to 5 years.

##### Leases

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

When a lease includes land and buildings elements, the bank assesses the classification of each element as either a finance lease or an operating lease. In determining classification of the land element, an important consideration is that land normally has an indefinite economic life. Therefore the finance lease or operating lease classification of the land is considered a critical area of judgment. See note 2(b) to these financial statements.

##### *The bank as lessor*

Assets held under finance leases are recognised as assets of the bank at their fair value at the date of acquisition. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation. Finance costs, which represent the difference between the total leasing commitments and the fair value of the assets acquired, are charged to the statement of comprehensive income over the term of the relevant lease so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

##### *The bank as lessee*

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

##### Impairment of non-financial assets

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

If objective evidence on impairment losses exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the profit or loss. In cases where the asset is carried at revalued amount, the impairment loss is treated as a revaluation decrease.

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 2 (a) ACCOUNTING POLICIES (Continued)

#### **Impairment of non-financial assets (Continued)**

In determining the recoverable amount, the bank considers the higher of the fair value of the asset less costs to sell, and value in use. In estimating value in use, the bank is cognisant of the estimated future cash flows discounted to the present value using a pre-tax discount rate that is reflective of the current market assessment of time value of money and the risks specific to the asset itself.

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

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

#### **Foreign currencies**

##### *i) Functional and presentation currency*

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

##### *ii) Transactions and balances*

Foreign currency transactions that are transactions denominated, or that requires settlement, in a foreign currency are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. At the reporting date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date.

Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

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

#### **Taxation**

Income tax expense represents the sum of the current tax payable and the deferred taxation.

Current taxation is provided on the basis of the results for the year, as shown in the financial statements, adjusted in accordance with tax legislation. Deferred taxation is provided using the liability method for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. Currently enacted tax rates are used to determine deferred taxation.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the unused tax credits can be utilised

#### **Financial instruments**

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

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 2 (a) ACCOUNTING POLICIES (Continued)

##### Financial instruments (Continued)

##### Financial assets

##### a) Classification and measurement

The bank classifies its financial assets into the following IAS 39 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 appropriate classification of its financial instruments at initial recognition, depending on the purpose and intention for which the financial instrument was acquired and their characteristics.

##### 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. Derivatives are also categorised as held for trading.

##### ii) *Due from banks and loans and receivables*

Due from banks and loans and receivables include non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are recognised when cash is advanced to borrowers.

After initial recognition, amounts 'Due from banks' and 'Loans and advances to customers' are subsequently measured at amortised cost using the effective interest rates, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The amortisation is included in 'Interest and similar income' in the profit and loss. The losses arising from impairment are recognised in profit or loss.

##### iii) *Held-to-maturity financial assets*

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the bank has the positive intention and ability to hold to maturity.

Held to maturity financial assets are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost using the effective interest method less any impairment, with revenue recognised on an effective yield basis. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate and recognised in the profit or loss.

Where a sale occurs other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and classified as available for sale. Furthermore, the bank would be prohibited from classifying any financial asset as held to maturity during the following two years.

##### vi) *Available-for-sale financial assets*

Available for sale investments are those that are 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 equity prices or that are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss.

Available-for-sale investments are initially recognised at fair value, which is the cash consideration including any transaction costs, and measured subsequently at fair value. Gains and losses arising from changes in fair value are recognised in other comprehensive income and accumulated in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest method, and foreign exchange gains and losses on monetary assets which are recognised in profit or loss.

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 2 (a) ACCOUNTING POLICIES (Continued)

#### Financial instruments (Continued)

#### Financial assets (Continued)

##### a) Classification and measurement (Continued)

###### vi) *Available-for-sale financial assets (Continued)*

Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously accumulated in the investments revaluation reserve is reclassified to profit or loss.

Dividends on available for sale equity instruments are recognised in profit and loss when the bank's right to receive the dividends is established.

##### b) Derecognition of financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired.
- the bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either:
- the bank has transferred substantially all the risks and rewards of the asset, or
- the bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the bank's continuing involvement in the asset. In that case, the bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the bank could be required to repay.

##### c) Impairment and uncollectability of financial assets

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

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

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 2 (a) ACCOUNTING POLICIES (Continued)

##### Financial instruments (Continued)

##### Financial assets (Continued)

##### c) Impairment and uncollectability of financial assets (Continued)

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

##### i) *Assets carried at amortised cost*

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial instruments effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss.

##### ii) *Loans and receivables*

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

Objective evidence that loans and receivables are impaired can include significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 30 days overdue), the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group are considered indicators that the loans or receivable is impaired.

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

##### a) **Individually assessed loans**

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

2 (a) ACCOUNTING POLICIES (Continued)

**Financial instruments (Continued)**

**Financial assets (Continued)**

*ii) Loans and receivables (continued)*

**b) Collectively assessed**

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

**Homogeneous groups of loans**

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

**Loan write – offs**

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

**Restructured loans**

Restructured loans, whose terms have been renegotiated are no longer considered to be past due but are treated as new loans after the minimum required number of payments under the new arrangement have been received.

*iii) Available-for-sale financial assets*

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

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

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 2 (a) ACCOUNTING POLICIES (Continued)

##### Financial instruments (Continued)

##### Financial liabilities and equity instruments issued by the bank

###### a) Classification and measurement

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

###### i) *Equity instruments*

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

###### ii) *Other financial liabilities*

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

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

###### b) Derecognition of financial liabilities

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

##### Offsetting

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

##### Provisions

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

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 2 (a) ACCOUNTING POLICIES (Continued)

#### **Statutory reserve**

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

#### **Cash and cash equivalents**

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

#### **Contingent liabilities**

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

#### **Fiduciary activities**

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

#### **Sale and repurchase agreements**

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

#### **Employee benefit costs**

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

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

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

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

#### **Comparatives**

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

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 2(b) CRITICAL JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the bank's accounting policies, which are described in note 2, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant including expectations of future events that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

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

The following are the critical judgements, apart from those involving estimations (see (ii) overleaf), that management have made in the process of applying the bank's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

###### *Impairment losses on loans and advances*

The bank reviews its loan portfolios to assess impairment regularly. In determining whether an impairment loss should be recorded in the profit and loss, the bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans, before a decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

###### *Classification of leases of land as finance or operating leases*

At the inception of each lease of land, the bank considers the substance rather than the form of the lease contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:

- The lease transfers ownership of the asset to the lessee by the end of the lease term;
- The lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised;
- The lease term is for the major part of the economic life of the asset even if title is not transferred;
- At the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and
- The leased assets are of such a specialised nature that only the lessee can use them without major modifications.

The bank also considers indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease. Examples of such indicators include:

- If the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
- gains or losses from the fluctuation in the fair value of the residual accrue to the lessee (for example, in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and
- the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 2(b) CRITICAL JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (Continued)

#### (i) Critical judgements in applying the banks accounting policies

##### *Impairment of available-for-sale investments*

The bank reviews its debt securities classified as available for sale investments at each reporting date to assess whether they are impaired. This requires similar judgment as applied to the individual assessment of loans and advances.

The bank also records impairment charges on available-for-sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is 'significant' or 'prolonged' requires judgment. In making this judgment, the bank evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investment is less than its cost.

##### *Held-to-maturity investments*

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

#### (ii) Key sources of estimation uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

##### *Property, equipment and intangible assets*

Critical estimates are made by management in determining depreciation rates for property, equipment and intangible assets.

##### *Fair value of trade receivables and payables*

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the bank for similar financial instruments.

##### *Taxation*

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

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 3 GOING CONCERN

As at 31 December 2015, the bank had a total regulatory capital/risk weighted assets ratio of 9.4% (2014: 10.97%) against a minimum required ratio of 14.5%. The bank therefore had not met the capital adequacy ratios and as a result, it was not issued with a banking licence. The issuance of the licence depends on conclusion of measures taken by directors to ensure compliance with the core capital requirements. The directors are taking the necessary measures to ensure compliance. As a result of the measures being taken by the directors, the National Treasury as one of the principal shareholders have so far injected Shs 500 million in additional capital to help reverse the situation. The bank is in the process of raising additional capital of Shs 1.8 billion through a rights issue which was approved by the shareholders during the Extra ordinary General Meeting held on 15 December 2015. The rights issue process is expected to be concluded on 4 April 2016.

#### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES

##### A. FINANCIAL RISK

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

##### *Risk management framework*

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

The board provides written principles for overall risk management as well as written policies covering specific risk areas. The bank's risk management policies are established to identify and analyse the risks faced by the bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and best market practices. The bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

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

The most important type of risks to which the bank is exposed to are financial risks which include:

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

##### (a) Credit risk

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

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

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

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

#### A. FINANCIAL RISK (Continued)

##### (a) Credit risk (continued)

###### Management of credit risk

The board of directors has delegated responsibility for the oversight of credit risk to its Finance and Credit Committee comprising of four non-executive directors. The implementation of the credit risk policies and monitoring of the credit portfolio to ensure that risks are managed within acceptable standards is the responsibility of the credit committee comprising of executive management. The committee assisted by the credit department is responsible for the management of the bank's credit risk including:

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

###### Credit risk measurement

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

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

The bank assesses the probability of default of individual borrowers using internal rating methods tailored to the various categories of the borrower. In assessing the credit quality of the customer the bank takes into account the customer's financial position, past experience and other industry specific factors. The credit risk measurements are embedded in the bank's daily operational management and closely aligned to the Central Bank of Kenya loan classifications. The impairment allowances on loans and advances computed through the bank's internal measures and the Central Bank of Kenya prudential guidelines are contrasted with the measurement of impairment under the IAS 39

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

#### A. FINANCIAL RISK (Continued)

##### (a) Credit risk (Continued)

###### **Risk limit control and mitigation policies**

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

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing limits where appropriate.

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

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

Commitments to extend credit represent unused portions of authorisation to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

A. FINANCIAL RISK (Continued)

(a) Credit risk (Continued)

Maximum exposure to credit risk before collateral held

|  | 2015                     |                   | 2014                     |                   |
|--|--------------------------|-------------------|--------------------------|-------------------|
|  | Sh'000                   | %                 | Sh'000                   | %                 |
| <b>Credit Exposures</b>  |                          |                   |                          |                   |
| <b>On – balance sheet items</b>  |                          |                   |                          |                   |
| Cash and balances with the CBK   | 759,717                  | 5                 | 1,406,318                | 9                 |
| Government securities  | 2,688,034                | 18                | 2,823,524                | 18                |
| Balances due from banking institutions   | 104,709                  | 1                 | 162,098                  | 1                 |
| Loans and advances to customers  | 9,221,256                | 62                | 9,212,581                | 60                |
|  | <u>12,773,716</u>        | <u>86</u>         | <u>13,604,521</u>        | <u>88</u>         |
| <b>Off-balance sheet items</b>   |                          |                   |                          |                   |
| Acceptances and letters of credit  | 39,620                   | 1                 | 99,302                   | 1                 |
| Guarantees   | 761,208                  | 5                 | 707,884                  | 5                 |
| Undrawn formal stand-by facilities, credit lines and other commitments to lend | 1,252,551                | 8                 | 916,946                  | 6                 |
|  | <u>2,053,379</u>         | <u>14</u>         | <u>1,724,132</u>         | <u>12</u>         |
| <b>At 31 December</b>  | <u><u>14,827,095</u></u> | <u><u>100</u></u> | <u><u>15,328,653</u></u> | <u><u>100</u></u> |

The above represents the worst case scenario of credit exposure for 31 December 2015 and 2014, without taking into account any collateral held or other credit enhancements attached. For on-balance sheet assets, the exposures, set out above are based on net carrying amount as reported on the statement of financial position.

Loans and advances to customers comprise of 62% (2014 - 60%) of the total maximum exposure. The fair value of collateral held in respect of assets subject to credit risk as at 31 Decembers 2015 was Sh 16,268,384,000 (2014- Sh 15, 711,536,125).

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

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

A. FINANCIAL RISK (Continued)

(a) Credit risk (Continued)

| Classification of loans and receivables           | Loans and advances<br>to customers |                |
|---|------------------------------------|----------------|
|   | 2015<br>Sh'000                     | 2014<br>Sh'000 |
| Carrying amount                                   |                                    |                |
| Individually impaired                             |                                    |                |
| Grade 6: Impaired (substandard)                   | 312,857                            | 475,014        |
| Grade 7: Impaired (doubtful)                      | 1,499,300                          | 2,316,799      |
| Grade 8: Impaired (loss)                          | 145,704                            | 18,687         |
|   | -----                              | -----          |
| Gross amount                                      | 1,957,861                          | 2,810,500      |
| Allowance for impairment                          | (479,550)                          | (1,074,002)    |
| Interest in suspense                              | (398,739)                          | (479,515)      |
|   | -----                              | -----          |
| Carrying amount                                   | 1,079,572                          | 1,256,983      |
|   | -----                              | -----          |
| Collectively impaired (past due but not impaired) |                                    |                |
| Grade 4-5: Watch list                             | 1,021,970                          | 904,685        |
| Allowance for impairment                          | (30,659)                           | (27,141)       |
|   | -----                              | -----          |
| Carrying amount                                   | 991,311                            | 877,544        |
|   | -----                              | -----          |
| Neither past due nor impaired                     |                                    |                |
| Grade 1-3: Normal                                 | 7,150,373                          | 7,078,054      |
|   | -----                              | -----          |
| Total carrying amount                             | 9,221,256                          | 9,212,581      |
|   | =====                              | =====          |

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

**Loans and receivables neither past due nor impaired**

The bank classifies loans and advances under this category for those exposures that are up to date and in line with contractual agreements. These exposures will normally be maintained within approved product programs and with no signs of impairment or distress. These exposures are categorised internally as grade 1-3, that is, normal accounts in line with CBK prudential guidelines and a provision of 1 % is made and appropriated from revenue reserves to statutory reserves.

**Loans and receivables past due but not impaired loans**

Loans where the contractual interest or principal payments are past due but the bank believes that impairment is not appropriate on the basis of the level of security/collateral available and/or the stage of collection of amounts owed to the bank are classified as past due but not impaired. These exposures are graded internally as category 4-5 that is watch accounts in the bank's internal credit risk grading system, in line with CBK guidelines.

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

A. FINANCIAL RISK (Continued)

(a) Credit risk (Continued)

Loans with renegotiated terms

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

Allowances for impairment

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

The internal credit risk grading system which is in line with CBK prudential guidelines focus on expected credit losses – that is taking into account the risk of future events giving rise to losses. In contrast, impairment allowances are recognised for financial reporting purposes only for losses that have been incurred at the date of the statement of financial position based on objective evidence of impairment. Due to the different methodologies applied, the amount of incurred credit losses provided for in the statement of comprehensive income is usually lower than the amount determined from the expected loss model that is used for internal operational management and banking regulation purposes.

Write-off policy

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

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

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

|   | Loans and advances<br>to customers |                |
|---|------------------------------------|----------------|
|   | 2015<br>Sh'000                     | 2014<br>Sh'000 |
| Against individually impaired<br>Property | 1,695,050                          | 1,998,295      |
| Against collectively impaired<br>Property | 1,995,622                          | 2,185,002      |
| Total                                     | 3,690,672                          | 4,183,297      |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

A. FINANCIAL RISK (Continued)

(a) Credit risk (Continued)

Settlement risk

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

Settlement limits form part of the credit approval/limit monitoring process described earlier. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals from bank Risk.

Concentration of risk

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

(i) Advances to customers- gross

|                             | 2015              |            | 2014              |            |
|-----------------------------|-------------------|------------|-------------------|------------|
|                             | Sh'000            | %          | Sh'000            | %          |
| Manufacturing               | 353,236           | 4          | 386,390           | 4          |
| Wholesale and retail        | 3,788,579         | 36         | 3,290,986         | 32         |
| Transport and communication | 1,288,804         | 12         | 735,348           | 7          |
| Agricultural                | 110,720           | 1          | 167,190           | 2          |
| Business services           | 135,367           | 1          | 304,388           | 3          |
| Real estate                 | 4,215,151         | 40         | 4,338,699         | 42         |
| Other                       | 637,087           | 6          | 1,090,723         | 10         |
|                             | <u>10,528,944</u> | <u>100</u> | <u>10,313,724</u> | <u>100</u> |

(ii) Customer deposits

|                                     |                  |            |                   |            |
|-------------------------------------|------------------|------------|-------------------|------------|
| Central and local Government        | 499,403          | 5          | 592,480           | 6          |
| Non-financial public enterprises    | 155,862          | 2          | 245,231           | 2          |
| Co-operative societies              | 1,782,118        | 18         | 2,009,231         | 18         |
| Insurance companies                 | 400,843          | 4          | 432,272           | 4          |
| Private enterprises and individuals | 6,946,413        | 69         | 7,203,805         | 68         |
| Non-profit institutions             | 211,419          | 2          | 158,940           | 2          |
|                                     | <u>9,996,058</u> | <u>100</u> | <u>10,641,959</u> | <u>100</u> |

(iii) Off balance sheet items  
(Letters of credit and guarantees)

|                             |                |            |                |            |
|-----------------------------|----------------|------------|----------------|------------|
| Manufacturing               | 10,150         | 1          | 3,742          | -          |
| Wholesale and retail        | 516,081        | 65         | 354,561        | 44         |
| Transport and communication | 38,018         | 5          | 11,304         | 2          |
| Business services           | 234,372        | 29         | 414,937        | 51         |
| Other                       | 2,207          | -          | 22,642         | 3          |
|                             | <u>800,828</u> | <u>100</u> | <u>807,186</u> | <u>100</u> |

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

#### A. FINANCIAL RISK (Continued)

##### (b) Liquidity risk

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

##### Management of liquidity risk

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

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

Liquidity risk is addressed through the following measures:

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

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

##### Exposure to liquidity risk

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

|                        | 2015 | 2014 |
|------------------------|------|------|
| At 31 December         |      |      |
| Average for the period | 32%  | 36%  |
| Maximum for the period | 34%  | 31%  |
| Minimum for the period | 36%  | 36%  |
|                        | 32%  | 23%  |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

A. FINANCIAL RISK (Continued)

(b) Liquidity risk (continued)

Liquidity risk based on undiscounted cash flows

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

| AT 31 DECEMBER 2015                               | Up to<br>1 month<br>Sh'000 | 1 – 3<br>months<br>Sh'000 | 4 - 12<br>months<br>Sh'000 | 1 - 5<br>Years<br>Sh'000 | Total<br>Sh'000   |
|---|----------------------------|---------------------------|----------------------------|--------------------------|-------------------|
| <b>FINANCIAL ASSETS</b>                           |                            |                           |                            |                          |                   |
| Cash and balances with the CBK                    | 603,035                    | 133,011                   | 25,304                     | -                        | 761,350           |
| Balances due from banking institutions            | 104,709                    | -                         | -                          | -                        | 104,709           |
| Government securities                             | -                          | 138,975                   | -                          | 2,763,180                | 2,902,155         |
| Loans and advances to customers                   | 1,890,748                  | 487,948                   | 2,384,435                  | 6,090,288                | 10,853,419        |
| <b>Total financial assets</b>                     | <b>2,598,492</b>           | <b>759,934</b>            | <b>2,409,739</b>           | <b>8,791,032</b>         | <b>14,621,633</b> |
| <b>FINANCIAL LIABILITIES</b>                      |                            |                           |                            |                          |                   |
| Deposits and balances due to banking institutions | 275,463                    | -                         | -                          | -                        | 275,463           |
| Customer deposits                                 | 5,739,236                  | 4,191,840                 | 763,292                    | -                        | 10,694,368        |
| Borrowed funds                                    | 99,121                     | 39,300                    | -                          | 2,061,563                | 2,199,984         |
| <b>Total financial liabilities</b>                | <b>6,113,820</b>           | <b>4,231,140</b>          | <b>763,292</b>             | <b>2,061,563</b>         | <b>13,169,815</b> |
| <b>Net liquidity gap</b>                          | <b>(3,515,328)</b>         | <b>(3,471,206)</b>        | <b>1,646,447</b>           | <b>6,729,469</b>         | <b>1,451,818</b>  |
| <b>AT 31 DECEMBER 2014</b>                        |                            |                           |                            |                          |                   |
| Total financial assets                            | 2,246,340                  | 565,018                   | 2,354,935                  | 10,384,541               | 15,550,834        |
| Total financial liabilities                       | 4,756,038                  | 246,519                   | 7,145,258                  | 2,892,791                | 15,040,606        |
| <b>Net liquidity gap</b>                          | <b>(2,509,698)</b>         | <b>318,499</b>            | <b>(4,790,323)</b>         | <b>7,491,750</b>         | <b>510,228</b>    |

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

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

#### A. FINANCIAL RISK (Continued)

##### (c) Market risks

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

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

##### **Management of market risks**

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

##### **Exposure to interest rate risk**

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates. The ALCO is the monitoring body for compliance with these limits and is assisted by Treasury Department in its day-to-day monitoring activities.

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

A. FINANCIAL RISK (Continued)

(c) Market risks (continued)

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

| AS AT 31 DECEMBER 2015                            | Up to<br>1 month<br>Sh'000 | 1 – 3<br>months<br>Sh'000 | 4 - 12<br>months<br>Sh'000 | 1 - 5<br>Years<br>Sh'000 | Non-<br>interest<br>bearing<br>Sh'000 | Total<br>Sh'000   |
|---|----------------------------|---------------------------|----------------------------|--------------------------|---------------------------------------|-------------------|
| <b>FINANCIAL ASSETS</b>                           |                            |                           |                            |                          |                                       |                   |
| Cash and balances with the CBK                    | -                          | -                         | -                          | -                        | 759,717                               | 759,717           |
| Balances due from other banking institutions      | 104,709                    | -                         | -                          | -                        | -                                     | 104,709           |
| Government securities                             | -                          | 138,975                   | -                          | 2,549,059                | -                                     | 2,688,034         |
| Loans and advances to customers                   | 9,221,256                  | -                         | -                          | -                        | -                                     | 9,221,256         |
| <b>Total financial assets</b>                     | <b>9,325,965</b>           | <b>138,975</b>            | <b>-</b>                   | <b>2,549,059</b>         | <b>759,717</b>                        | <b>12,773,716</b> |
| <b>FINANCIAL LIABILITIES</b>                      |                            |                           |                            |                          |                                       |                   |
| Deposits and balances due to banking institutions | 275,463                    | -                         | -                          | -                        | -                                     | 275,463           |
| Customer deposits                                 | 1,171,694                  | 4,526,392                 | 1,772,059                  | -                        | 2,525,913                             | 9,996,058         |
| Borrowed funds                                    | 99,121                     | 39,300                    | -                          | 1,830,873                | -                                     | 1,969,294         |
| <b>Total financial liabilities</b>                | <b>1,546,278</b>           | <b>4,565,692</b>          | <b>1,772,059</b>           | <b>1,830,873</b>         | <b>2,525,913</b>                      | <b>12,240,815</b> |
| <b>Interest rate sensitivity gap</b>              | <b>7,779,687</b>           | <b>(4,426,717)</b>        | <b>(1,772,059)</b>         | <b>718,186</b>           | <b>(1,766,196)</b>                    | <b>532,901</b>    |
| <b>AS AT 31 DECEMBER 2014</b>                     |                            |                           |                            |                          |                                       |                   |
| Total financial assets                            | 9,374,679                  | 143,515                   | -                          | 2,680,009                | 1,406,318                             | 13,604,521        |
| Total financial liabilities                       | 1,758,228                  | 370,302                   | 6,348,097                  | 1,782,111                | 2,970,866                             | 13,229,604        |
| <b>Interest rate sensitivity gap</b>              | <b>7,616,451</b>           | <b>(226,787)</b>          | <b>(6,348,097)</b>         | <b>897,898</b>           | <b>(1,564,548)</b>                    | <b>374,917</b>    |

**Currency Risk**

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

CONSOLIDATED BANK OF KENYA LIMITED  
 NOTES TO THE FINANCIAL STATEMENTS (Continued)  
 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

A. FINANCIAL RISK (Continued)

(c) Market risks (continued)

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

| AS AT 31 DECEMBER 2015                          | KSH<br>Sh'000     | USD<br>Sh'000  | GBP<br>Sh'000 | EURO<br>Sh'000   | OTHERS<br>Sh'000 | TOTAL<br>Sh'000   |
|---|-------------------|----------------|---------------|------------------|------------------|-------------------|
| <b>FINANCIAL ASSETS</b>                         |                   |                |               |                  |                  |                   |
| Cash and balances with Central Bank of Kenya    | 680,877           | 32,753         | 4,174         | 41,863           | 50               | 759,717           |
| Balances due from Banking institutions          | 61,374            | 24,232         | 7,386         | 11,475           | 242              | 104,709           |
| Government securities                           | 2,688,034         | -              | -             | -                | -                | 2,688,034         |
| Loans and advances to customers                 | 8,878,595         | 342,661        | -             | -                | -                | 9,221,256         |
| <b>Total financial assets</b>                   | <b>12,308,880</b> | <b>399,646</b> | <b>11,560</b> | <b>53,338</b>    | <b>292</b>       | <b>12,773,716</b> |
| <b>FINANCIAL LIABILITIES</b>                    |                   |                |               |                  |                  |                   |
| Deposits & balances due to banking institutions | 224,363           | 51,100         | -             | -                | -                | 275,463           |
| Customer deposits                               | 9,687,519         | 286,675        | 6,531         | 15,334           | -                | 9,996,058         |
| Borrowed funds                                  | 1,729,552         | -              | -             | 239,742          | -                | 1,969,294         |
| <b>Total financial liabilities</b>              | <b>11,641,434</b> | <b>337,775</b> | <b>6,531</b>  | <b>255,076</b>   | <b>-</b>         | <b>12,240,816</b> |
| <b>NET ON BALANCE SHEET POSITION</b>            | <b>667,446</b>    | <b>61,871</b>  | <b>5,029</b>  | <b>(201,738)</b> | <b>292</b>       | <b>532,900</b>    |
| <b>NET OFF BALANCE SHEET POSITION</b>           | <b>744,077</b>    | <b>106,559</b> | <b>7,617</b>  | <b>46,940</b>    | <b>-</b>         | <b>905,193</b>    |
| <b>AT 31 DECEMBER 2014</b>                      |                   |                |               |                  |                  |                   |
| Total financial assets                          | 13,181,226        | 338,440        | 56,288        | 24,496           | 4,071            | 13,604,521        |
| Total financial liabilities                     | 12,646,862        | 274,871        | 4,691         | 303,180          | -                | 13,229,604        |
| <b>NET ON BALANCE SHEET POSITION</b>            | <b>534,364</b>    | <b>63,569</b>  | <b>51,597</b> | <b>(278,684)</b> | <b>4,071</b>     | <b>374,917</b>    |
| <b>NET OFF BALANCE SHEET POSITION</b>           | <b>774,117</b>    | <b>179,837</b> | <b>44,528</b> | <b>2,629</b>     | <b>448</b>       | <b>1,001,559</b>  |

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

#### A. FINANCIAL RISK (Continued)

##### (c) Market risks (continued)

##### Market risks - sensitivity analysis

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

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

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

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

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

The table below sets out the impact on future net interest income of an incremental 10% parallel fall or rise in all yield curves at the beginning of each quarter during the 12 months from 1 January 2015.

|                               | Amount<br>31 December 2015<br>Sh'000 | Scenario 1<br>10% appreciation<br>Sh'000 | Scenario 2<br>10% Depreciation<br>Sh'000 |
|-------------------------------|--------------------------------------|--|--|
| Profit Before Tax             | 48,789                               | 150,672                                  | (53,094)                                 |
| Adjusted Core Capital         | 1,090,056                            | 1,919,939                                | 988,173                                  |
| Adjusted Total Capital        | 1,316,292                            | 1,418,175                                | 1,214,409                                |
| Risk Weighted Assets (RWA)    | 13,973,956                           | 13,973,956                               | 13,973,956                               |
| Adjusted Core Capital to RWA  | 7.8%                                 | 8.5%                                     | 7.1%                                     |
| Adjusted total Capital to RWA | 9.4%                                 | 10.1%                                    | 8.7%                                     |

Assuming no management actions, a series of such appreciation would increase net interest income for 2015 by Sh 101, 882,900 (2014 - Sh 91,314,000), while a series of such falls would decrease net interest income for 2015 by Sh 101,882,900 (2014 -Sh 107, 506,300).

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

A. FINANCIAL RISK (Continued)

(c) Market risks (continued)

Market risks - sensitivity analysis (Continued)

Also a series of such rises would increase the adjusted core capital to RWA and Adjusted total capital to RWA by 0.7% (2014: 1.3%) and 0.7% (2014: 1.3%) respectively, while a series of such falls would decrease the adjusted core capital to RWA and Adjusted total capital to RWA by 0.7% (2014: 0.7%) and 0.7% (2014: 0.7%) respectively..

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

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

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

The table below sets out the impact on future earnings of an incremental 10% parallel fall or rise in all foreign currencies at the beginning of each quarter during the 12 months from 1 January 2015.

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

|                               | Amount<br>31 December 2015<br>Sh'000 | Scenario 1<br>10% appreciation<br>Sh'000 | Scenario 2<br>10% Depreciation<br>Sh'000 |
|-------------------------------|--------------------------------------|--|--|
| Profit Before Tax             | 48,789                               | 52,452                                   | 45,126                                   |
| Adjusted Core Capital         | 1,090,056                            | 1,093,719                                | 1,086,393                                |
| Adjusted Total Capital        | 1,316,292                            | 1,319,955                                | 1,312,629                                |
| Risk Weighted Assets (RWA)    | 13,973,956                           | 13,973,956                               | 13,973,956                               |
| Adjusted Core Capital to RWA  | 7.8%                                 | 7.8%                                     | 7.8%                                     |
| Adjusted total Capital to RWA | 9.4%                                 | 9.4%                                     | 9.4%                                     |

Assuming no management actions, a series of such appreciation would increase earnings for 2015 by Sh.3, 662,800 (2014 - Sh 4, 379,600), while a series of such falls would decrease earning for 2015 by Sh.3, 662,800 (2014 - Sh4, 379,600).

Also a series of such rises would increase the adjusted core capital to RWA and Adjusted total capital to RWA by,0.0 % (2014 - 0.0%) and 0.0% (2014 - 0.1 %) respectively, while a series of such falls would decrease the adjusted core capital to RWA and Adjusted total capital to RWA by 0.0% (2014 - 0.1%) and 0.0% (2014 - 0%) respectively.

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

#### B. OTHER RISKS

##### Non-financial risk management disclosures:

##### a) Strategic risk

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

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

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

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

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

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

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

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

**B. OTHER RISKS (Continued)**

**Non-financial risk management disclosures:**

**b) Operational risk**

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

The major operational risks faced by the bank include.

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

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

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

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

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

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

- Robust operational Risk Policy and procedures that reflects industry practice are put in place and operationalized. These include toolkits to help identify, assess, control, manage and report on key Operational Risks. Toolkits in the Operational Risk Procedures manual include inter alia:
  - i) Framework for the Bank, businesses, and support functions to identify their major Operational Risks and mitigation plans,
  - ii) Key control standards,

# CONSOLIDATED BANK OF KENYA LIMITED

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

#### B. OTHER RISKS (Continued)

##### Non-Financial Risk Management disclosures:

##### b) Operational risk (Continued)

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

##### c) Compliance (policy/legal/regulatory) risk:

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

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

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

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

**B. OTHER RISKS (Continued)**

**d) Reputational risk**

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

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

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

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

**C. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES**

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

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

**31 December 2015**

Financial assets held for trading.

| Note                    | Level   | Level   | Level   | Total   |
|-------------------------|---------|---------|---------|---------|
|                         | 1       | 2       | 3       |         |
|                         | Shs'000 | Shs'000 | Shs'000 | Shs'000 |
| Quoted investments      | 6,879   | -       | -       | 6,879   |
|                         | 6,879   | -       | -       | 6,879   |
| <b>31 December 2014</b> |         |         |         |         |
| Quoted investments      | 3,906   | -       | -       | 3,906   |
|                         | 3,906   | -       | -       | 3,906   |

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 4 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

##### C. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (Continued)

The above were valued at quoted bid prices in an active market (Nairobi Securities Exchange).

Except as detailed above, the directors consider that the carrying amounts of financial assets and financial liabilities recognised in the statement of financial position approximate their fair values.

This note provides information about how the bank determines fair values of various financial assets and financial liabilities.

Fair value of the bank's financial assets and liabilities that are measured at fair value on a recurrent basis

Some of the bank's financial assets and financial liabilities are measured at fair value at the end of each reporting period. The following table gives information about how the fair values of these financial assets and financial liabilities are determined (in particular, the valuation technique(s) and inputs used):

| <i>Financial assets/liabilities</i> | <i>Fair value as at</i> |                     | <i>Fair value hierarchy</i> | <i>Valuation technique (s) and key inputs</i> | <i>Significant unobservable inputs</i> | <i>Relationship of unobservable inputs to fair value</i> |
|-------------------------------------|-------------------------|---------------------|-----------------------------|---|--|--|
|                                     | 31/12/15<br>Shs '000    | 31/12/14<br>Shs'000 |                             |   |  |  |
| Quoted investments                  | 6,011                   | 3,906               | Level 1                     | Quoted bid prices in an active market         | N/A                                    | N/A  |

There were no transfers between levels 1, 2 and 3 in the period (2014: none).

##### *Reconciliation of level 3 fair value measurements*

There were no financial assets or financial liabilities measured at fair value on level 3 fair value measurements (2014: none)

#### 5 CAPITAL MANAGEMENT

##### **Regulatory capital**

The banks objectives when managing capital are:

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

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

The Central Bank of Kenya requires each bank to:

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

5 CAPITAL MANAGEMENT (Continued)

Institutions that met the previous minimum capital ratios of 8% and 12% but remain below the buffer-enhanced ratios of 10.5% and 14.5% had until 31 December 2014 to comply. The Bank had not complied with this requirement as at 31 December 2015 and 31 December 2014.

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

- Tier 1 capital, which includes ordinary share capital, non-cumulative irredeemable non-convertible preference shares, disclosed reserves such as share premiums, retained earnings, and 50% un-audited after tax profit less investment in subsidiaries conducting banking business, investments in equity of other institutions, intangible assets (excluding computer software ) and goodwill.
- Tier 2 capital, which includes 25% revaluation surplus which have received prior CBK approval, subordinated debt, hybrid capital instruments or any other capital instruments approved by CBK.

The bank's regulatory capital position at 31 December 2015 and 31 December 2014 was as follows:

|  | 2015<br>Sh'000   | 2014<br>Sh'000   |
|--|------------------|------------------|
| <b>Tier 1 capital</b>  |                  |                  |
| Ordinary share capital   | 898,400          | 398,400          |
| Capital awaiting allocation  | -                | 500,000          |
| Non-cumulative irredeemable shares   | 721,130          | 721,130          |
|  | -----            | -----            |
| Share capital  | 1,619,530        | 1,619,530        |
| Accumulated deficit  | (533,841)        | (531,528)        |
|  | -----            | -----            |
| <b>Total</b>   | <b>1,085,689</b> | <b>1,088,002</b> |
|  | -----            | -----            |
| <b>Tier 2 capital</b>  |                  |                  |
| Revaluation reserves (25%)   | 99,093           | 77,034           |
| General loan loss provision (statutory reserve)  | 127,143          | 70,781           |
| Subordinated debt  | -                | 207,838          |
|  | -----            | -----            |
| <b>Total</b>   | <b>226,236</b>   | <b>355,653</b>   |
|  | -----            | -----            |
| <b>Total regulatory capital</b>  | <b>1,311,925</b> | <b>1,443,655</b> |
|  | =====            | =====            |
| Risk-weighted assets   | 13,973,956       | 13,138,981       |
|  | -----            | -----            |
| <b>Capital ratios:</b>   |                  |                  |
| Total regulatory capital expressed as a percentage of total risk-weighted assets (CBK minimum 14.5%) | 9.40%            | 10.97%           |
| Total tier 1 capital expressed as a percentage of risk-weighted assets (CBK minimum 8%)              | 7.78%            | 8.27%            |
|  | -----            | -----            |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

|    | 2015<br>Sh'000  | 2014<br>Sh'000                      |
|----|---|-------------------------------------|
| 6  | INTEREST INCOME   |                                     |
|    | 1,729,428   | 1,809,167                           |
|    | Interest on loans and advances  | Interest on bank placements         |
|    | 6,470   | 12,515                              |
|    | 221,516   | 232,855                             |
|    | Interest on government securities - Held to maturity  |                                     |
|    | <u>1,957,414</u>  | <u>2,054,537</u>                    |
|    | =====   | =====                               |
| 7  | INTEREST EXPENSE  |                                     |
|    | 634,718   | 860,254                             |
|    | Interest on customer deposits   | Interest on inter-bank borrowings   |
|    | 57,838  | 29,595                              |
|    | 246,029   | 251,547                             |
|    | Interest on borrowed funds  |                                     |
|    | <u>938,585</u>  | <u>1,141,396</u>                    |
|    | =====   | =====                               |
| 8  | FEE AND COMMISSION INCOME   |                                     |
|    | 55,060  | 58,618                              |
|    | Ledger related fees and commissions   | Credit related fees and commissions |
|    | 130,433   | 123,209                             |
|    | 131,372   | 140,059                             |
|    | Transaction related fees  |                                     |
|    | <u>316,865</u>  | <u>321,886</u>                      |
|    | =====   | =====                               |
| 9  | FOREIGN EXCHANGE INCOME – NET   |                                     |
|    | Foreign exchange net income includes gains and losses from spot and forward contracts and translated foreign currency assets and liabilities. |                                     |
|    | 2015<br>Sh'000  | 2014<br>Sh'000                      |
| 10 | OTHER OPERATING INCOME  |                                     |
|    | 11,721  | 26,889                              |
|    | Gain on bond trading  | Rental income                       |
|    | 65,637  | 60,535                              |
|    | Loss on written off software  | -                                   |
|    | -   | (719)                               |
|    | 564,220   | 2,315                               |
|    | Recoveries on loans and advances  | Sundry income                       |
|    | 1,135   | 13,278                              |
|    | <u>642,713</u>  | <u>102,298</u>                      |
|    | =====   | =====                               |

CONSOLIDATED BANK OF KENYA LIMITED  
 NOTES TO THE FINANCIAL STATEMENTS (Continued)

|   | 2015<br>Sh'000   | 2014<br>Sh'000   |
|---|------------------|------------------|
| 11 OPERATING EXPENSES   |                  |                  |
| Staff costs (note 12)   | 711,921          | 644,383          |
| Directors' emoluments - Fees  | 13,197           | 17,401           |
| - Other   | 15,124           | -                |
| Depreciation (note 22)  | 104,599          | 109,159          |
| Amortisation of intangible assets (note 23)                                       | 60,771           | 31,973           |
| Amortisation of operating lease (note 24)   | 170              | 170              |
| Contribution to Kenya Deposit Insurance Corporation                               | 17,775           | 19,879           |
| Auditors' remuneration  | 4,158            | 3,960            |
| Other operating expenses  | 449,847          | 380,614          |
|   | <u>1,377,562</u> | <u>1,207,539</u> |
| 12 STAFF COSTS  |                  |                  |
| Salaries and wages  | 578,223          | 526,860          |
| Training, recruitment and staff welfare costs                                     | 44,160           | 36,531           |
| Pension contributions   | 35,731           | 34,326           |
| Medical expenses  | 37,534           | 32,437           |
| Leave pay provision   | 5,598            | 8,503            |
| Staff insurance   | 6,938            | 5,015            |
| Gratuity provision  | 3,042            | -                |
| NSSF contributions  | 695              | 711              |
|   | <u>711,921</u>   | <u>644,383</u>   |
| 13 TAXATION   |                  |                  |
| a) Taxation charge  |                  |                  |
| Current tax based on the taxable profit for the year at 30%                       | 7,300            | 17,696           |
| Deferred tax charge/(credit) (note 27)  | 15,607           | (74,620)         |
| Prior year (over)/under provision- current taxation                               | (858)            | 55,949           |
| Prior year (over)/under provision- deferred taxation                              | (17,682)         | 8,417            |
|   | <u>4,367</u>     | <u>7,442</u>     |
| b) Reconciliation of expected tax based on accounting profit/(loss) to tax charge |                  |                  |
| Profit/(loss) before taxation   | 47,789           | (274,190)        |
| Tax calculated at a tax rate of 30%   | 14,637           | (82,257)         |
| Tax effect of expenses not deductible for tax purposes                            | 10,070           | 27,133           |
| Non-taxable income  | (1,800)          | (1,800)          |
| Prior year (over)/under provision- current taxation                               | (858)            | 55,949           |
| Prior year (over)/under provision- deferred taxation                              | (17,682)         | 8,417            |
|   | <u>4,367</u>     | <u>7,442</u>     |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

13 TAXATION (CONTINUED)

|                                   | 2015<br>Sh'000 | 2014<br>Sh'000 |
|-----------------------------------|----------------|----------------|
| c) Taxation recoverable           |                |                |
| At 1 January                      | 6,300          | 79,945         |
| Charge for the year               | (7,300)        | (17,696)       |
| Prior year over/(under) provision | 858            | (55,949)       |
| Tax paid during the year          | 12,307         | -              |
|                                   | <u>12,165</u>  | <u>6,300</u>   |
| At 31 December                    | <u>12,165</u>  | <u>6,300</u>   |

14 EARNINGS/(LOSS) PER SHARE

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

|   | 2015   | 2014      |
|---|--------|-----------|
| Profit/(loss) for the year (Sh'000)             | 44,422 | (281,632) |
| Number of ordinary shares (number in thousands) | 44,920 | 19,920    |
| <b>Earnings/(loss) per share</b>                |        |           |
| Basic and diluted (Sh)                          | 0.99   | (14.14)   |

There were no potentially dilutive shares outstanding as at 31 December 2015 and 31 December 2014, respectively. Diluted earnings per share are therefore the same as basic earnings per share.

15 CASH AND BALANCES WITH CENTRAL BANK OF KENYA

|  | 2015<br>Sh'000 | 2014<br>Sh'000   |
|--|----------------|------------------|
| Cash in hand                                     | 360,933        | 477,031          |
| Balances with Central Bank of Kenya:             |                |                  |
| - Cash ratio reserve                             | 342,851        | 568,282          |
| - Other balances (available for use by the bank) | 55,933         | 361,005          |
|  | <u>759,717</u> | <u>1,406,318</u> |
|  | <u>759,717</u> | <u>1,406,318</u> |

Cash in hand and balances with Central Bank of Kenya are non-interest bearing. The cash ratio reserve is based on the value of customer deposits as adjusted by the Central Bank of Kenya requirements. As at 31 December 2015 the cash ratio reserve requirement was 5.25% (2014 – 5.25%) of all customer deposits held by the bank. These funds are not available to finance the bank's day to day operations.

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

|  | 2015<br>Sh'000 | 2014<br>Sh'000 |
|--|----------------|----------------|
| 16 DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS             |                |                |
| a) Balances due from banking institutions maturing within 90 days: |                |                |
| Balances with correspondent banks                                  | 54,709         | 162,098        |
| Balances with local banks  | 50,000         | -              |
|  | <u>104,709</u> | <u>162,098</u> |
| b) Balances due to banking institutions maturing within 90 days:   |                |                |
| Deposits from local banks  | 275,463        | 533,502        |
|  | <u>275,463</u> | <u>533,502</u> |

Deposits with/from local banks as at 31 December 2015 represent overnight lending. The effective interest rate on deposits due from and due to local banking institutions at 31 December 2015 was 12.34% (2014 – 6.24%) and nil (2014–0.387%) for balances with correspondent banks

|  | 2015<br>Sh'000   | 2014<br>Sh'000   |
|--|------------------|------------------|
| 17 GOVERNMENT SECURITIES                                     |                  |                  |
| a) HELD TO MATURITY  |                  |                  |
| Treasury bonds –at amortised cost                            | 2,688,034        | 2,823,524        |
|  | <u>2,688,034</u> | <u>2,823,524</u> |
| The maturity profile of government securities is as follows: |                  |                  |
| Less than 1 year   | 138,975          | 143,515          |
| 3 years to 5 years   | 92,114           | 100,093          |
| Over 5 years   | 2,456,945        | 2,579,916        |
|  | <u>2,688,034</u> | <u>2,823,524</u> |

The weighted average effective interest rate on treasury bonds was 8.4% (2014 –8 3%).

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

|  | 2015<br>Sh'000 | 2014<br>Sh'000 |
|--|----------------|----------------|
| 18 LOANS AND RECEIVABLES                             |                |                |
| (a) Commercial loans                                 | 3,938,853      | 4,394,940      |
| Overdrafts   | 1,434,106      | 1,459,407      |
| Mortgages  | 2,632,763      | 2,900,564      |
| Asset finance loans                                  | 1,122,914      | 827,332        |
| Staff loans  | 602,829        | 731,481        |
|  | <hr/>          | <hr/>          |
| Gross loans and receivables                          | 9,731,465      | 10,313,724     |
| Less:  |                |                |
| Impairment losses on loans and receivables (note 19) | (510,209)      | (1,101,143)    |
|  | <hr/>          | <hr/>          |
| Net loans and receivables                            | 9,221,256      | 9,212,581      |
|  | <hr/> <hr/>    | <hr/> <hr/>    |

The weighted average effective interest rate on loans and receivables as at 31 December 2015 was 17.9% (2014 – 18.3%).

Included in gross loans and receivables of Sh 9,731,465,000 (2014 – Sh 10,313,724,000) are non-performing loans amounting to Sh 1,558,664,000 (2014 – Sh 2,330,985,000). These are included in the statement of financial position net of specific provisions of Sh 479,550,000 (2014 – Sh 1,074,002,000).

|   | 2015<br>Sh'000 | 2014<br>Sh'000 |
|---|----------------|----------------|
| (b) Analysis of gross loans and receivables by maturity |                |                |
| Maturing:   |                |                |
| Within 1 year   | 4,295,461      | 3,224,518      |
| Between 1 and 3 years                                   | 1,564,129      | 2,273,209      |
| After 3 years   | 3,871,875      | 4,815,997      |
|   | <hr/>          | <hr/>          |
| Loans and receivables to customers                      | 9,731,465      | 10,313,724     |
|   | <hr/> <hr/>    | <hr/> <hr/>    |

The related party transactions and balances are covered under note 37 and concentration of advances to customers is covered under note 4.

19 IMPAIRMENT LOSSES ON LOANS AND RECEIVABLES

|                                   | 2015<br>Sh'000 | 2014<br>Sh'000 |
|-----------------------------------|----------------|----------------|
| At 1 January                      | 1,101,143      | 743,990        |
| Increase in impairment allowances | 588,684        | 447,772        |
| Write offs                        | (617,838)      | (90,619)       |
| Recoveries                        | (561,780)      | -              |
|                                   | <hr/>          | <hr/>          |
| At 31 December                    | 510,209        | 1,101,143      |
|                                   | <hr/> <hr/>    | <hr/> <hr/>    |

CONSOLIDATED BANK OF KENYA LIMITED  
 NOTES TO THE FINANCIAL STATEMENTS (Continued)

|   | 2015<br>Sh'000 | 2014<br>Sh'000 |
|---|----------------|----------------|
| 20 OTHER ASSETS                               |                |                |
| Un-cleared items in the course of collection  | 24,638         | 34,685         |
| Prepayments                                   | 39,274         | 31,384         |
| Rent receivable                               | 8,599          | 7,063          |
| Deposits for services                         | 15,015         | 13,955         |
| Others  | 162,960        | 148,228        |
|   | <u>250,486</u> | <u>235,315</u> |
| 21 QUOTED EQUITY SHARES -- AVAILABLE FOR SALE |                |                |
| At beginning of the year                      | 3,906          | 2,061          |
| Gain in market value of investment            | 2,973          | 1,845          |
|   | <u>6,879</u>   | <u>3,906</u>   |

The investment consists of 21,699 shares of Kakuzi Limited which are in the name of Jimba Credit Corporation Limited, a dormant subsidiary company.

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

22 PROPERTY AND EQUIPMENT

|  | Freehold<br>land and<br>buildings<br>Sh'000 | Leasehold<br>improvements<br>Sh'000 | Motor<br>vehicles<br>Sh'000 | Fixtures,<br>fittings,<br>equipment<br>& ATMs<br>Sh'000 | Computers<br>Sh'000 | Total<br>Sh'000  |
|--|---|-------------------------------------|-----------------------------|---|---------------------|------------------|
| COST/VALUATION                         |   |                                     |                             |   |                     |                  |
| At 1 January 2014                      | 647,000                                     | 405,165                             | 17,988                      | 303,336   | 125,882             | 1,499,371        |
| Additions                              | -   | 387                                 | -                           | 4,207   | 5,071               | 9,665            |
| Reclassification                       | -   | -                                   | -                           | (3,949)   | 3,949               | -                |
| Surplus on revaluation                 | 72,000                                      | -                                   | -                           | -   | -                   | 72,000           |
| At 31 December 2014                    | <u>719,000</u>                              | <u>405,552</u>                      | <u>17,988</u>               | <u>303,594</u>  | <u>134,902</u>      | <u>1,581,036</u> |
| At 1 January 2015                      | 719,000                                     | 405,552                             | 17,988                      | 303,594   | 134,902             | 1,581,036        |
| Additions                              | -   | 308                                 | -                           | 6,373   | 4,650               | 11,331           |
| Reclassification-<br>intangible assets | -   | -                                   | -                           | -   | (2,550)             | (2,550)          |
| At 31 December 2015                    | <u>719,000</u>                              | <u>405,860</u>                      | <u>17,988</u>               | <u>309,967</u>  | <u>137,002</u>      | <u>1,589,817</u> |
| Comprising                             |   |                                     |                             |   |                     |                  |
| At cost                                | -   | 405,860                             | 17,988                      | 309,967   | 137,002             | 870,817          |
| At valuation 2014                      | 719,000                                     | -                                   | -                           | -   | -                   | 719,000          |
|  | <u>719,000</u>                              | <u>405,860</u>                      | <u>17,988</u>               | <u>309,967</u>  | <u>137,002</u>      | <u>1,589,817</u> |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 PROPERTY AND EQUIPMENT (Continued)

|                                 | Freehold<br>land and<br>buildings<br>Sh'000 | Leasehold<br>improvements<br>Sh'000 | Motor<br>vehicles<br>Sh'000 | Fixtures,<br>fittings,<br>equipment &<br>ATMs<br>Sh'000 | Computers<br>Sh'000 | Total<br>Sh'000 |
|---------------------------------|---|-------------------------------------|-----------------------------|---|---------------------|-----------------|
| <b>ACCUMULATED DEPRECIATION</b> |   |                                     |                             |   |                     |                 |
| At 1 January 2014               | 63,868                                      | 254,765                             | 14,424                      | 220,770   | 59,637              | 613,464         |
| Charge for the year             | 15,425                                      | 40,635                              | 1,316                       | 23,338  | 28,445              | 109,159         |
| Reclassification                | -   | -                                   | -                           | (36,179)  | 36,179              | -               |
| Eliminated on revaluation       | (79,293)                                    | -                                   | -                           | -   | -                   | (79,293)        |
| At 31 December 2014             | -   | 295,400                             | 15,740                      | 207,929   | 124,261             | 643,330         |
| At 1 January 2015               | -   | 295,400                             | 15,740                      | 207,929   | 124,261             | 643,330         |
| Charge for the year             | 17,225                                      | 41,678                              | 999                         | 31,798  | 12,899              | 104,599         |
| Transferred on reclassification | -   | -                                   | -                           | -   | (2,550)             | (2,550)         |
| At 31 December 2015             | 17,225                                      | 337,078                             | 16,739                      | 239,727   | 134,610             | 745,379         |
| <b>NET BOOK VALUE</b>           |   |                                     |                             |   |                     |                 |
| At 31 December 2015             | 701,775                                     | 68,782                              | 1,249                       | 70,240  | 2,392               | 844,438         |
| At 31 December 2014             | 719,000                                     | 110,152                             | 2,248                       | 95,665  | 10,641              | 937,706         |

Freehold land and buildings were last revalued as at 31 December 2014, by Vidmerck Limited, independent Valuers. Valuations were made on the basis of the open market value using the highest and best use valuation model resulting in a total valuation surplus of Sh 151,293,000. The book values of the properties were adjusted to the revalued amounts and the resultant surplus was credited to the revaluation surplus.

Motor vehicles, fixtures fittings and equipment with a cost of Sh 419, 038,164 (2014- Sh 405, 012,633) were fully depreciated as at 31 December 2015. The notional annual depreciation charge on these assets would have been Sh 84, 673,625 (2014- Sh 74, 064,546).

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

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

|                     | 2015<br>Sh'000 | 2014<br>Sh'000 |
|---------------------|----------------|----------------|
| At 1 January        | 140,160        | 144,681        |
| Depreciation charge | (4,521)        | (4,521)        |
| At 31 December      | 135,639        | 140,160        |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

|    | 2015<br>Sh'000                                   | 2014<br>Sh'000                              |
|----|--|---|
| 23 | INTANGIBLE ASSETS – COMPUTER SOFTWARE            |   |
|    | COST   |   |
|    |  | At 1 January                                |
|    | 332,946  | 309,906                                     |
|    |  | Additions                                   |
|    | 19,482   | 27,976                                      |
|    |  | Reclassification                            |
|    | 2,550  | (4,936)                                     |
|    |  | Impaired                                    |
|    | -  | (4,936)                                     |
|    | 354,978  | 332,946                                     |
|    | ACCUMULATED AMORTISATION                         |   |
|    |  | At 1 January                                |
|    | 50,962   | 23,206                                      |
|    |  | Charge for the year                         |
|    | 60,771   | 31,973                                      |
|    |  | Reclassification/(eliminated) on impairment |
|    | 2,550  | (4,217)                                     |
|    | 114,283  | 50,962                                      |
|    | NET BOOK VALUE                                   |   |
|    |  | At 31 December                              |
|    | 240,695  | 281,984                                     |
| 24 | PREPAID OPERATING LEASE RENTALS (LEASEHOLD LAND) |   |
|    | COST   |   |
|    |  | At 1 January and 31 December                |
|    | 45,298   | 45,298                                      |
|    | ACCUMULATED AMORTISATION                         |   |
|    |  | At 1 January                                |
|    | 37,979   | 37,809                                      |
|    |  | Charge for the year                         |
|    | 170  | 170   |
|    | 38,149   | 37,979                                      |
|    | NET BOOK VALUE                                   |   |
|    |  | At 31 December                              |
|    | 7,149  | 7,319                                       |
| 25 | CUSTOMER DEPOSITS                                |   |
|    |  | Current and demand accounts                 |
|    | 2,480,424  | 3,239,130                                   |
|    |  | Savings accounts                            |
|    | 1,171,694  | 1,302,249                                   |
|    |  | Fixed deposit accounts                      |
|    | 6,298,451  | 6,050,484                                   |
|    |  | Margins                                     |
|    | 45,489   | 50,096                                      |
|    | 9,996,058  | 10,641,959                                  |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

|    | 2015<br>Sh'000                         | 2014<br>Sh'000    |
|----|--|-------------------|
| 25 | CUSTOMER DEPOSITS (Continued)          |                   |
|    | MATURITY ANALYSIS OF CUSTOMER DEPOSITS |                   |
|    | Repayable:                             |                   |
|    | On demand                              | 3,697,607         |
|    | Within one year                        | 4,541,379         |
|    |  | 6,100,580         |
|    | <u>9,996,058</u>                       | <u>10,641,959</u> |

The weighted average effective interest rate on interest bearing customer deposits at 31 December 2015 was 7.2% (2014 – 9.3%). The related party transactions and balances are covered under note 37 and concentration of customers' deposits is covered under note 4.

|    | 2015<br>Sh'000         | 2014<br>Sh'000 |
|----|------------------------|----------------|
| 26 | OTHER LIABILITIES      |                |
|    | Accrued expenses       | 5,824          |
|    | Gratuity               | 3,042          |
|    | Leave pay provision    | 10,892         |
|    | Tenants deposits       | 15,741         |
|    | Cheques for collection | 329            |
|    | Sundry payables        | 204,993        |
|    |                        | 240,821        |
|    |                        | 3,513          |
|    |                        | -              |
|    |                        | 8,503          |
|    |                        | 14,867         |
|    |                        | 2,633          |
|    |                        | 209,359        |
|    | <u>240,821</u>         | <u>238,875</u> |

27 DEFERRED TAX LIABILITY

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

|  | 2015<br>Sh'000                      | 2014<br>Sh'000   |
|--|-------------------------------------|------------------|
|  | <i>Deferred tax assets:</i>         |                  |
|  | General bad debts provision         | (1,573)          |
|  | Provision for leave pay             | (3,268)          |
|  | Provision for gratuity              | (912)            |
|  | Provision for fraud                 | (5,527)          |
|  | Accelerated depreciation allowances | (1,575)          |
|  | Tax losses                          | (116,569)        |
|  |                                     | (129,423)        |
|  |                                     | (17,252)         |
|  |                                     | (2,551)          |
|  |                                     | -                |
|  |                                     | -                |
|  |                                     | -                |
|  |                                     | (117,018)        |
|  | <u>(129,423)</u>                    | <u>(136,821)</u> |
|  | <i>Deferred tax liabilities:</i>    |                  |
|  | Revaluation surplus                 | 168,100          |
|  | Accelerated capital allowances      | -                |
|  |                                     | 5,347            |
|  |                                     | 177,573          |
|  | <u>168,100</u>                      | <u>177,573</u>   |
|  |                                     | 38,677           |
|  |                                     | 40,752           |
|  | <u>38,677</u>                       | <u>40,752</u>    |

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

27 DEFERRED TAX LIABILITY (Continued)

|   | 2015<br>Sh'000 | 2014<br>Sh'000 |
|---|----------------|----------------|
| Movement in deferred tax liability is as follows: |                |                |
| At 1 January                                      | 40,752         | 61,567         |
| Credit to profit or loss (note 13)                | 15,607         | (74,620)       |
| Charged to other comprehensive income             | -              | 45,388         |
| Prior year (over)/under provision (note 13)       | (17,682)       | 8,417          |
| At 31 December                                    | <u>38,677</u>  | <u>40,752</u>  |

As at 31 December 2015, the bank had accumulated tax losses amounting to Sh 388,564,039 (2014 –Sh 449,087,000) available to be offset against future taxable profit. Under Kenyan legislation, tax losses can only be carried forward to a maximum of four years.

|                                    | 2015<br>Sh'000       | 2014<br>Sh'000       |
|------------------------------------|----------------------|----------------------|
| 28 BORROWINGS                      |                      |                      |
| As 1 January                       |                      |                      |
| Accrued interest                   | 2,054,143            | 2,099,497            |
| Repayments during the year         | 246,029<br>(330,878) | 252,074<br>(297,428) |
| At the end of the year             | <u>1,969,294</u>     | <u>2,054,143</u>     |
| <i>Analysis by currency:</i>       |                      |                      |
| Borrowings in Euros                | 239,742              | 281,487              |
| Borrowings in Kenya Shillings (Sh) | 1,729,552            | 1,772,656            |
|                                    | <u>1,969,294</u>     | <u>2,054,143</u>     |
| <i>Analysis by lender:</i>         |                      |                      |
| European Investment Bank (EIB)     | 239,742              | 281,487              |
| Corporate bond – medium term notes | 1,729,552            | 1,772,656            |
|                                    | <u>1,969,294</u>     | <u>2,054,143</u>     |

**Facility terms:**

- a) EIB Loan facility: The facility from European investment bank was credit line of Eur 6,500,000 received by the bank as part of its participation in the global loan facility extended by EIB to a group of financial institutions in Kenya under the Cotonou Agreement. The facility terms are as follows
- Tenure: The tenor of the financing which shall be between 4 to 10 years save in respect of sub-loans for small projects where the sub loan is less than the equivalent of EUR 50,000 and finance leases, which shall have a minimum tenor of 3 years
  - Interest rate: For a tranche denominated in EUR or Usd as margin of 2.88% per annum and for tranches denominated in Kenya shillings will attract additional currency risk premium depending on the tenor of the loan
  - Security: a negative pledge on present and future business undertakings together with all the assets or revenues of the bank

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (Continued)

28 BORROWINGS (Continued)

Facility terms: (Continued)

- b) Medium term notes: this refers to a series of senior and subordinated notes issued by the bank and traded on the Nairobi Securities Exchange. The issued and currently traded notes have a face value Sh 1,678,200,000.
- Tenor: the notes mature on 22 July 2019
  - Interest rate: the notes attract a fixed interest rate of 13.5 % for the senior notes and 13.25% for the subordinated notes

|   | 2015<br>Sh'000   | 2014<br>Sh'000   |
|---|------------------|------------------|
| 29 SHARE CAPITAL  |                  |                  |
| a) Authorised:  |                  |                  |
| 55,000,000 ordinary shares of Sh 20 each  | 1,100,000        | 400,000          |
| 80,000,000 4% non-cumulative irredeemable non-convertible preference shares of Sh 20 each | 1,600,000        | 1,600,000        |
|   | <u>2,700,000</u> | <u>2,000,000</u> |
| b) Issued and fully paid:   |                  |                  |
| 44,920,000 ordinary shares of Sh 20 each (2014 – 19,920,000)                              | 898,400          | 398,400          |
| 36,056,500 4% non-cumulative irredeemable Non-convertible preference shares of Sh 20 each | 721,130          | 721,130          |
|   | <u>1,619,530</u> | <u>1,119,530</u> |
| c) Capital awaiting allotment:  |                  |                  |
| As at 1 January   | 500,000          | -                |
| Received in the year  | -                | 500,000          |
| Allotted in the year  | (500,000)        | -                |
|   | <u>-</u>         | <u>500,000</u>   |

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

On 15 December 2015, the additional capital of Ksh.500 million received from the National Treasury on 11 December 2014 and previously held as capital awaiting allotment was allotted as 25,000,000 additional shares during the extra ordinary meeting of the shareholders.



CONSOLIDATED BANK OF KENYA LIMITED  
 NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

|     | 2015<br>Sh'000  | 2014<br>Sh'000        |
|-----|---|-----------------------|
| 34  | NOTES TO THE STATEMENT OF CASH FLOWS  |                       |
| (a) | Reconciliation of profit/(loss) before taxation to cash used in operations                                      |                       |
|     | Profit/(loss) before taxation   | 48,789 (274,190)      |
|     | Adjustments for:  |                       |
|     | Depreciation of property and equipment (note 22)  | 104,599 109,159       |
|     | Amortisation of intangible assets (note 23)   | 60,771 31,973         |
|     | Amortisation of leasehold land (note 24)  | 170 170               |
|     | Loss on written off software  | - 719                 |
|     | Profit/(loss) before working capital changes  | 214,329 (132,169)     |
|     | Decrease/(increase) in cash ratio balance   | 225,431 (14,065)      |
|     | (Increase)/decrease in other assets   | (15,171) 19,816       |
|     | (Increase)/decrease in loans and receivables  | (8,675) 1,642,911     |
|     | Decrease in customer deposits   | (645,901) (1,069,138) |
|     | Increase in other liabilities   | 1,946 (159,690)       |
|     | Decrease in treasury bonds  | 135,490 512,053       |
|     | Accrued interest on borrowings (note 28)  | 246,029 252,074       |
|     | Cash generated from operations  | 153,478 1,051,792     |
| (b) | Analysis of the balances of cash and cash equivalents as shown in the statement of financial position and notes |                       |
|     | Cash in hand  | 360,933 477,031       |
|     | Balances with Central Bank of Kenya –other  | 55,933 361,005        |
|     | Balances with other banking institutions  | 104,709 162,098       |
|     | Deposits and balances from other banking institutions   | (275,463) (533,502)   |
|     | 246,112   | 466,632               |

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

CONSOLIDATED BANK OF KENYA LIMITED  
 NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

35 INVESTMENTS IN SUBSIDIARIES

The subsidiary companies of Consolidated Bank of Kenya Limited are:

- Jimba Credit Corporation Limited
- Kenya Savings & Mortgages Limited
- Citizen Building Society
- Estate Building Society
- Estate Finance Company of Kenya Limited
- Business Finance Company Limited
- Home Savings and Mortgages Limited
- Union Bank of Kenya Limited
- Nationwide Finance Company Limited

All the subsidiaries are dormant and are wholly owned by the bank.

The operations of the above companies were vested in the bank in July 2002. Because of the insignificance of the amounts involved, the directors are of the opinion that consolidation of these subsidiaries would be of no real value.

36 CONTINGENCIES AND COMMITMENTS INCLUDING OFF BALANCE SHEET ITEMS

a) **Contingent liabilities**

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

|                                   | 2015<br>Sh'000 | 2014<br>Sh'000   |
|-----------------------------------|----------------|------------------|
| Acceptances and letters of credit | 39,620         | 99,302           |
| Guarantees                        | 761,208        | 707,884          |
| Forwards and spot contingents     | 104,365        | 194,373          |
|                                   | <u>905,193</u> | <u>1,001,559</u> |
| Litigations against the bank      | 41,175         | 2,019            |

Nature of contingent liabilities:

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

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

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

Concentrations of contingent liabilities are covered under note 4.

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

36 CONTINGENCIES AND COMMITMENTS INCLUDING OFF BALANCE SHEET ITEMS (CONTINUED)

|  | 2015<br>Sh'000 | 2014<br>Sh'000 |
|--|----------------|----------------|
| <b>b) Commitments to extend credit</b>   |                |                |
| Undrawn formal stand-by facilities, credit lines and other commitments to lend | 1,252,551      | 916,946        |

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

|                                   | 2015<br>Sh'000 | 2014<br>Sh'000 |
|-----------------------------------|----------------|----------------|
| <b>c) Capital commitments</b>     |                |                |
| Authorised but not contracted for | 481,092        | 121,610        |

Capital commitments relate to, construction of five new branches, data storage upgrade, core banking enhancement and three branch renovations.

**d) Operating lease commitments**

Rental income earned during the year was Sh 65, 636,988 (2014 – Sh 60,434,555). At the reporting date, the bank had contracted with tenants for the following minimum future lease receivables:

|                                       | 2015<br>Sh'000 | 2014<br>Sh'000 |
|---------------------------------------|----------------|----------------|
| <i>The bank as a lessor.</i>          |                |                |
| Within one year                       | 60,830         | 57,936         |
| In the second to fifth year inclusive | 168,628        | 149,311        |
| After five years                      | 420            | 1,166          |
|                                       | <u>229,878</u> | <u>208,413</u> |

Leases are negotiated for an average term of 6 years and rentals are reviewed every two years. The leases are cancellable with a penalty when the tenants do not give three months' notice to vacate the premises.

*The bank as a lessee*

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

|                                       | 2015<br>Sh'000 | 2014<br>Sh'000 |
|---------------------------------------|----------------|----------------|
| Within one year                       | 41,813         | 52,969         |
| In the second to fifth year inclusive | 183,062        | 190,283        |
| After five years                      | 18,364         | 36,824         |
|                                       | <u>243,239</u> | <u>280,076</u> |

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

CONSOLIDATED BANK OF KENYA LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

37 RELATED PARTY TRANSACTIONS

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

Placings are made in the bank by directors, their associates and companies associated to directors. Advances to customers at 31 December 2015 include advances and loans to companies associated with the directors. Contingent liabilities at 31 December 2015 include guarantees and letters of credit for companies associated with the directors.

All transactions with related parties are at arm's length in the normal course of business, and on terms and conditions similar to those applicable to other customers.

|  | Directors      |                |
|--|----------------|----------------|
|  | 2015<br>Sh'000 | 2014<br>Sh'000 |
| Movement in related party balances was as follows: |                |                |
| <i>Loans and advances:</i>                         |                |                |
| At 1 January                                       | -              | -              |
| Advanced during the year                           | 7,300          | -              |
| Interest earned                                    | 71             | -              |
| Repaid during the year                             | (525)          | -              |
| At 31 December                                     | <u>6,846</u>   | <u>-</u>       |

As at 31 December 2015 loans and advances to staff amounted to Sh 602,984,650 (2014– Sh 791,010,350).

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

|                                    | Directors      |                |
|------------------------------------|----------------|----------------|
|                                    | 2015<br>Sh'000 | 2014<br>Sh'000 |
| <i>Customer deposits:</i>          |                |                |
| At 1 January                       | -              | -              |
| Placed during the year             | 2,300          | -              |
| Net interest applied               | -              | -              |
| Withdrawals                        | -              | -              |
| At 31 December                     | <u>2,300</u>   | <u>-</u>       |
| <b>Key management compensation</b> | <u>2,300</u>   | <u>-</u>       |

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

|                                |                |                |
|--------------------------------|----------------|----------------|
| Salaries and other benefits    | 92,140         | 86,884         |
| Fees for services as directors | 13,197         | 17,401         |
|                                | <u>105,337</u> | <u>104,285</u> |

## CONSOLIDATED BANK OF KENYA LIMITED

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 38 INCORPORATION

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

#### 39 CURRENCY

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

#### 40 EVENTS AFTER THE REPORTING DATE

No material events or circumstances have arisen between the reporting date and the date of this report that require disclosure.