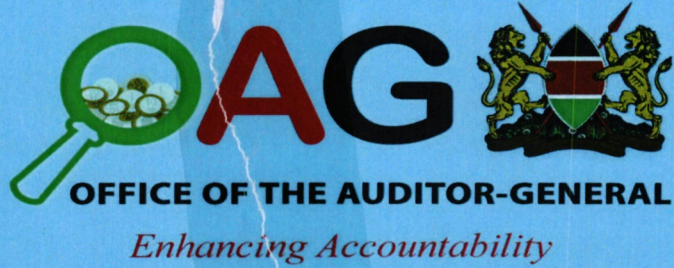


REPUBLIC OF KENYA



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REPORT

OF

THE AUDITOR-GENERAL

ON

**DEVELOPMENT BANK OF
KENYA LIMITED**

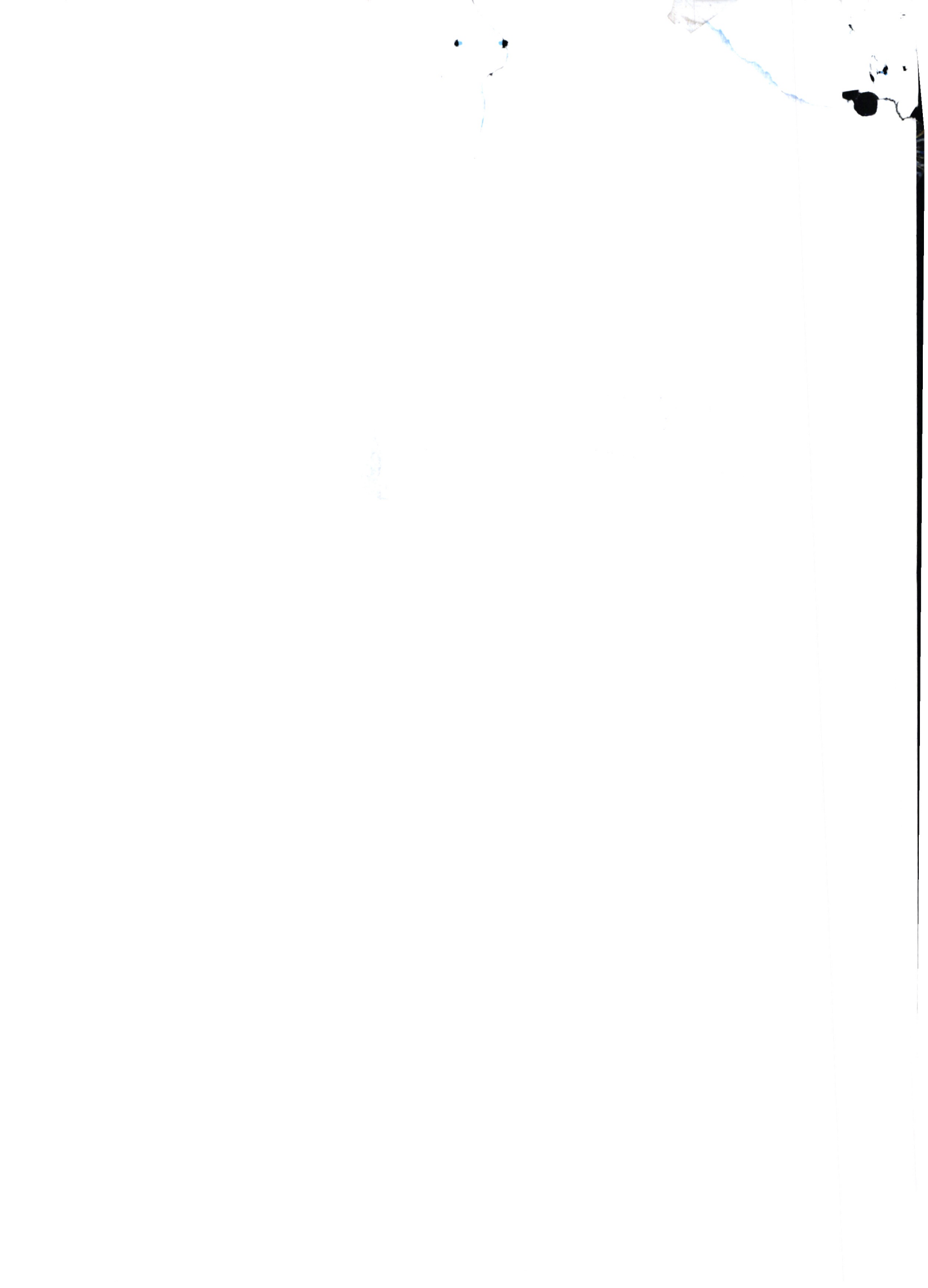
**FOR THE YEAR ENDED
31 DECEMBER, 2020**

THE NATIONAL ASSEMBLY
PAPERS LAIN

DATE: 05 AUG 2021

TABLED BY: The Majority Whip
Hon. E. Wangwe

THAT TABLES: Mainah wanjiku




OFFICE OF THE AUDITOR GENERAL
P. O. Box 30084 - 00100, NAIROBI
REGISTRY
30 MAR 2021
RECEIVED

DEVELOPMENT BANK OF KENYA LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2020


THE NATIONAL ASSEMBLY
PAPERS LAID
DATE: 05 AUG 2021
TABLED BY:
CLERK AT THE TABLE:

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Registered office

Finance House
Loita Street
PO Box 30483, 00100
Telephone: (254) 020 340401/2/3
Email: dbk@devbank.com
Telegrams: DEVBANK.KE
Nairobi
Kenya

Subsidiary

Small Enterprises Finance Company Limited (SEFCO)
PO Box 34045 - 00100
Telephone: (254) 020 340401/2/3
Telex: 22662
Nairobi
Kenya

Shareholders

Industrial & Commercial Development Corporation (ICDC)
PO Box 45519 - 00100
Nairobi
Kenya

TransCentury Plc
PO Box 42588 - 00100
Nairobi
Kenya

Directors

The directors who served during the year and to the date of this report are:

Haggai William – Chairman
Ndung'u Gathinji
Victor Kidiwa
Sammy Kipkosgei Chepkwony
Jackson Kambo Mutua
Rose Wangui Mambo
Industrial & Commercial Development Corporation (ICDC)
Cabinet Secretary to the Treasury of Kenya

Secretary

C.A. Otieno (Mrs)
Finance House
Loita Street
PO Box 30483 - 00100
Nairobi, GPO

Senior officers

V. J. O. Kidiwa	Chief Executive
J. K. Kiniti	Chief Finance Officer
C. Otieno	Company Secretary
O. Sechero	Manager Credit
D. Nyaboke	Manager Legal
J. Manager	Relationship Manager
D. Kamunde	Business Development
D. Namwendwa	Human Resource Manager
F. Ouma	Internal Audit manager
P. Pertet	Risk and Compliance Manager
B. Kakule	Operations Manager
E. Anguka	Treasury Manager
W. Ogada	IT Manager

Auditor

KPMG Kenya 8 th Floor, ABC Towers Waiyaki Way PO Box 40612 - 00100 Nairobi GPO	<i>On behalf of:</i>	The Auditor-General Kenya National Audit Office Anniversary Towers University Way PO Box 30084 - 00100 Nairobi GPO
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Correspondent banks

Standard Chartered Bank One Madison Avenue New York, 10010 - 3603 USA	Nedbank PO Box 1144 Johannesburg 2000, GTG South Africa
Standard Chartered Bank 1 Basinghall Avenue London EC2V 5DD Tel +44 (020) 7885 8888	Standard Chartered Bank 90 Matatma Gandhi Road Mumbai India 400 001 Tel. + 91 22 226 70162
BHF Bank Bockenheimer Landstrasse 10 D – 60323 Frankfurt Am Main Germany	Bank of Communications China 188 Yin Cheng Zhong Road Shangai 200120 - China Tel: + 86 21 58408478

Development Bank of Kenya Limited
Five year financial summary
For the year ended 31 December 2020

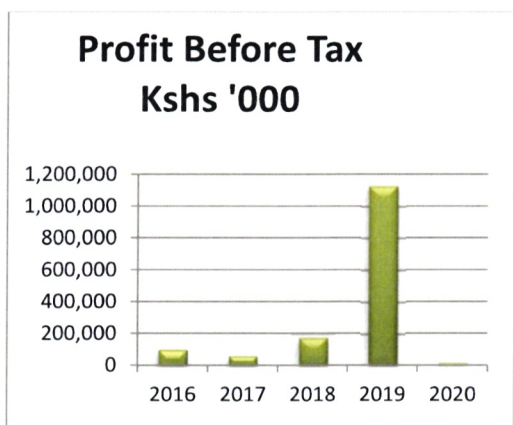
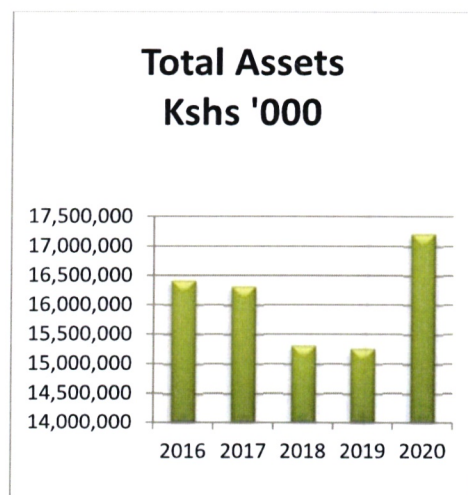
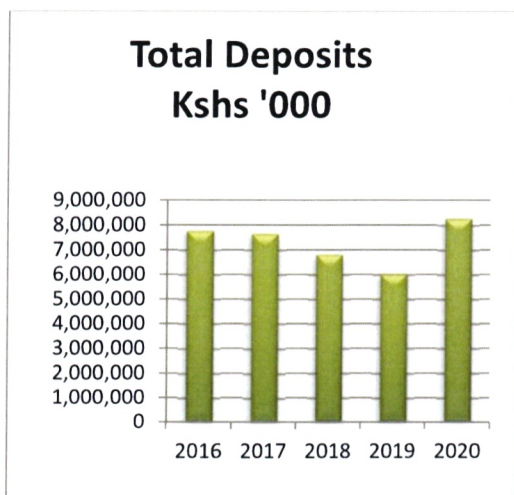
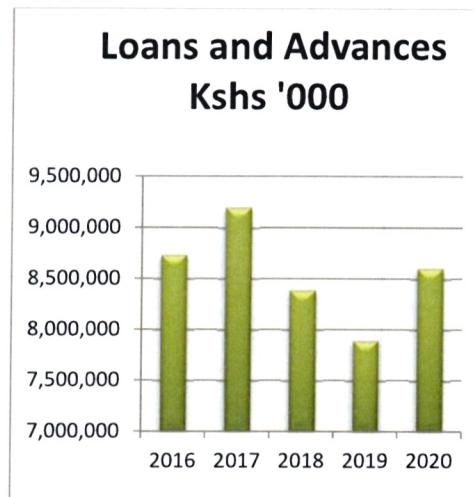
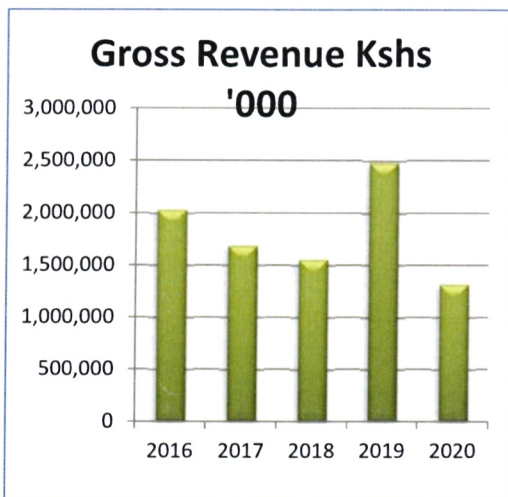
Five-year Group financial summary

	2020	2019	2018	2017	2016
	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000
Gross revenue	1,317,916	2,479,788	1,551,617	1,684,587	2,031,005
Profit before tax	20,541	1,139,192	170,767	59,426	97,755
Profit after tax	21,830	1,080,773	115,813	27,658	61,715
Gross loans and advances	10,189,074	9,409,288	9,862,729	10,312,685	9,823,634
Less impairment losses on loans and advances	(1,579,785)	(1,498,242)	(1,476,042)	(1,112,906)	(1,090,422)
Loans and advances to customers (net of impairment)	8,609,289	7,911,046	8,386,697	9,199,779	8,733,212
Total deposits	8,252,500	6,003,890	6,799,074	7,643,952	7,760,936
Borrowings	4,672,533	4,877,168	5,037,465	5,435,938	5,472,728
Shareholders' equity	3,840,513	3,967,043	2,886,270	2,943,323	2,915,665
Total assets	17,214,197	15,350,170	15,312,605	16,309,056	16,411,435

KEY RATIOS

Basic Earnings Per Share (EPS)	0.42	20.73	2.22	0.53	1.18
Return on Assets (ROA)	0.13%	7.04%	0.76%	0.17%	0.38%
Return on Equity (ROE)	0.57%	26.88%	4.01%	0.94%	2.12%
Capital Adequacy Ratio	19.8%	28.2%	19.90%	20.10%	21.60%

KEY PERFORMANCE INDICATORS



Introduction

It is with great pleasure that I present to you the Annual report and financial statements of Development Bank of Kenya limited (DBK) and its wholly owned subsidiary Small Enterprises Finance Company (SEFCO).

Year 2020 was a fairly challenging year not just locally but also globally. The advent of Covid-19, a global health pandemic presented the entire World with a challenge of epic proportion. The world had not known a pandemic of Covid-19 proportion since the influenza flu in 1919. The effects of Covid – 19 shook the fabric of World economies in a significant way. Most of the countries, besides locking their economies had to spend huge sums of money to deal with the adverse effects of this disease.

It is against this background that I present the financials for the year 2020.

Economic Overview

According to the most recent economic survey by the World Bank, the global economy is projected to have contracted by 4.3% in 2020 due to the challenges emanating from the Covid-19 pandemic. The counter measures against Covid - 19 pandemic included economic shut down of most of the leading economies. This explains the contraction of the global economy. For the year 2021, the World Bank projects the global economic expansion of 4.0% assuming an initial Covid-19 vaccine rollout becomes widespread throughout the year. This “recovery, however will likely be subdued unless policy makers move more decisively to tame the pandemic and implement investment enhancing reforms”, the World Bank says in its January 2021 *Global Economic prospects*.

Based on data from the Kenya Bureau of Statistics (KBS), Kenya's economic growth averaged 5.7% in 2019 compared to a similar growth rate in 2018 and 4.9% achieved in 2017. In 2020, however, real Gross Domestic Product (GDP) is expected to have decelerated to 1.5%. This is on the back of depressed economic activity driven by the shutdown occasioned by Covid- 19 pandemic. Prior to this, the economy had been expected to expand by 5.9%.

In order to ameliorate the negative effects of the pandemic, the government introduced various measures cutting across a number of sectors. Among the measures were those directed at the banking sector such as the revision of the Central bank borrowing Rate (CBR) to 7.00% from 8.25%, the reduction of cash reserve ratio from 5.25% to 4.25% and the suspension of referring loans that become delinquent with effect from 2 March from being reported to Credit Reference Bureau (CRB). More specifically, customers whose businesses had been affected adversely were allowed to seek suspension of repayments with their banks without such loans being downgraded. It should be noted that without the above measures, the impact of Covid – 19 on the Banking sector results for 2020 would have been severely depressed.

Developments in the Banking Sector

The banking sector remained stable and resilient in 2020. According to the Monetary Policy Committee (MPC), over the six months to October, the average commercial banks liquidity and capital adequacy ratios remained strong above the statutory requirements. The ratio of gross non-performing loans (NPLs) to gross loans stood at 13.6 percent in October 2020, largely reflecting low business activity in sectors affected by the COVID-19 pandemic.

Despite the adverse effects of the pandemic, credit to the private sector remained resilient, growing by 7.7 percent in the 12 months to October 2020. This was supported by improved liquidity conditions and decline in lending rates due to the impact of the accommodative monetary policy stance adopted by the MPC. In June 2020, CBK extended the banking sector emergency measures issued in March to continue supporting the economy. The CBK also closely monitored the implementation of these measures, while ensuring that the interbank market and liquidity management across the sector continued to function smoothly.

Developments in the Banking Sector (Continued)

According to the Central bank of Kenya’s credit survey for the fourth quarter of 2020, the sector pre-tax profit fell by a third or KShs 46 billion to KShs 112.8 billion. This was on the back of a sharp rise in non-performing loans and depressed revenues owing to their connection to most economic players in the market. Non – performing loans ratio is expected to rise further to around 16% unless the economy recovers quickly.

The DBK’s Performance

DBK has been on a recovery mode since 2016 when it was severely affected by the closure of a number of banks in the country resulting in panic withdrawal of customer deposits from tier III banks. The various strategies developed by the Board and management have started bearing fruit with the sale of finance house in 2019, improving the Banks liquidity significantly. As at the end of December 2020, the Bank’s liquidity stood at 22.6% against the minimum 20% required by Central Bank. This means that the bank is now complying with all the ratios set by the Regulator.

The bank’s business in 2020 was steady despite the tough operating environment brought about by the counter measure employed by government to contain Covi-19 pandemic. The Bank registered overall growth in assets from KShs 15.4 billion at the end of 2019 to KShs 17.2 billion at December 2020. This was brought about by increased customer deposits from KShs 5.1 billion to KShs 6.2 billion or 21.6% growth. This increase in assets was achieved in spite of the bank having settled KShs 600 million of the debt owed to the Central Bank of Kenya. The group’s profit after tax, at KShs 21.8 million was however significantly lower than the outturn of 2019 at KShs 1,080.8 million. 2019 profit before tax factored in a one-off profit from sale of Finance House of KShs 1,062.0 million. Besides this, 2020 profit before tax was heavily affected by reduced interest income on the back of increased non-performing loans.

The gross loan portfolio increased by 7.0% from KShs 9.4 billion to KShs 10.2 billion achieved in 2020. After adjusting for additional provisions against non-performing loans, the net loans closed higher at KShs 8.6 billion compared to KShs 7.9 billion.

The bulk of credit was advanced to the real estate and trade investments as shown below.

SECTOR	Portfolio 2020	Portfolio 2019
Agriculture	9.4%	8.7%
Manufacturing	17.6%	16.5%
Building & Construction	2.0%	2.5%
Trade	27.7%	29.1%
Tourism, Restaurants, Hotels	3.5%	3.2%
Transport & Communication	3.3%	3.2%
Real Estate	33.0%	31.3%
Financial Services	0.2%	0.3%
Personal Households	3.4%	5.2%
TOTAL	100.0%	100.0%

Appreciation

I take this opportunity to express my sincere gratitude to all our esteemed clients for their continued support and confidence that they have expressed in us during these challenging times. I also wish to thank my fellow directors, management and staff of the group for their able stewardship of the group without which it would have been difficult to achieve the results we have.

Haggai William
 Chairman



Date: 15 March 2021

The Shareholders being the ultimate owners of the Bank appoint a Board of Directors to conduct the business of the bank on their behalf. The Board executes its responsibilities through Management and Board Committees that it creates from time to time. The responsibilities for daily operations are delegated to a management team appointed by the Board. A clear segregation of responsibilities between the Board and management is always maintained. The Board makes all policy decisions while management implements the decisions of the Board.

Board of Directors

The current Board is made up of six directors inclusive of a non-executive chairman.

Board and Management Committees

Tabulated below are Board and Management Committees, their composition and membership and functions.

	Composition & Membership	Chairman	Members	Main Functions
Board Audit Committee	Three Non-Executive Directors, and Senior Management	Independent Director	Sammy Chepkwony - Chair Ndung'u Gathinji Jackson Mutua F. Ouma – Internal auditor C. A. Otieno (Mrs) Management (by invitation)	Independent oversight of the bank Financial reporting and internal control systems, checks and balances
Board Credit Committee	Three non-Executive Directors, and Senior Management	Independent Director	Jackson Mutua - Chair Mbatha Mbithi Felix Oulo V. Kidiwa J. Mananda Olga Sechero C. A. Otieno (Mrs)	Reviewing and overseeing the overall lending in the Bank
Board Risk & compliance Committee	Three Non-Executive Directors and Senior Management	Independent Director	Rose Mambo - Chair Haggai Williams Jackson Mutua V. Kidiwa J. Kiniti C. A. Otieno (Mrs) Peter Pertet	To ensure quality, integrity and reliability of the institution's risk management, compliance, IT Governance and Strategy.
Governance & Nomination Committee	Three Non-Executive Directors and Senior Management	Non-Executive Director	Ndung'u Gathinji - Chair Mbatha Mbithi Rose Mambo V. Kidiwa C. A. Otieno (Mrs) Dorcas Namwendwa	Oversight of the quality of governance in the Bank and HR matters

Board and Management Committees (Continued)

	Composition & Membership	Chairman	Members	Main Functions
Strategy, Business Development & IT Committee	Three Non-Executive Directors and Senior Management	Non-Executive Director	Sammy Chepkwony – Chair Haggai Williams Felix Oulo V. Kidiwa J Kiniti D. Kamunde W. Ogada C. A. Otieno (Mrs)	To oversee the development, formulation and implementation of the Bank’s strategy and to develop the Bank’s long term I T Strategy

Board attendance

Prudential regulations require that every Board member attend a minimum of 75% of all Board meetings. Below is an extract from the attendance register for the Board meetings held in 2020:

Names	Jan 29	Mar 6	Jun 16	July 29	AGM Oct 7	Oct 29	Nov 16-17	Dec 9	% Attendance
William Haggai	X	X	X	X	X	X	X	X	100
Ndung’u Gathinji	X	X	X	X	X	X	X	X	100
Mbatha Mbithi	-	X	X	X	X	X	X	X	88
Sammy Chepkwony	X	X	X	X	X	X	X	X	100
Jackson Mutua	-	X	X	X	X	X	X	X	88
Rose Mambo	-	-	X	X	X	X	X	X	75

Directors Evaluation Report

It is a requirement that the performance of every Director and the Chairman of the Board be evaluated once every year. Evaluation of directors’ performance is underway and is expected to be complete before 31 March 2021.

The directors submit their report together with the audited financial statements for the year ended 31 December 2020.

BUSINESS REVIEW

The group is engaged in the business of development and commercial banking. It is licensed under the Kenyan Banking Act.

The performance of the Bank in 2020 was on the backdrop of the Covid-19 Pandemic which affected the global economy as well as the Kenyan economy. The pandemic led to disruptions in community health, business and trade in and across borders, affecting different sectors of the economy in various ways.

Since the Bank's customers were impacted by the pandemic, the bank has restructured various facilities with customers in order to support them navigate through the economic disruptions. The restructure of facilities included extension of repayments and moratorium for certain periods. The bank will continue to work with customers to offer them the necessary relief. On its part, the government intervened by reducing the corporate tax rate for the year from 30% to 25% to cushion businesses from the adverse effects of the pandemic.

The ongoing Covid-19 pandemic has also increased the estimation uncertainty in the preparation of the financial statements. The Bank has made various estimates for future events in the financial statements based on forecasts of economic conditions which reflect expectations and assumptions as at 31 December 2020 and which the Bank believes are reasonable under the circumstances. There is a considerable degree of judgement involved in preparing these estimates. The underlying assumptions are also subject to uncertainties which are often outside the control of the Bank. Accordingly, actual economic conditions are likely to be different from those forecast since anticipated events do not occur as expected, and the effect of those differences may significantly impact accounting estimates included in the financial statements.

The principal risks and uncertainties facing the Bank include credit risk, liquidity risk, market risks, operational risks and settlement risk. The Bank has mitigation plans and strategies for these risks as detailed in Note 4 of these financial statements.

During the year 2020, the Group recorded a profit of KShs 21.8 million which is significantly lower than the previous year's profit of KShs 1,080.8 million. The decrease was mainly due to a one-off profit on sale of Finance House recorded in 2019.

Total assets amounted to KShs 17.2 billion (2019 – KShs 15.4 billion). Loan portfolio rose from Kshs 7.9 million in 2019 to KShs 8.6 billion at the close of 2020. The quality of the portfolio as measured by the non-performing ratio to the gross loan book improved from 35.9% (2019) to 33.7% (2020). Total deposits increased by 37.4% to KShs 8.3 billion (2019: KShs 6.0 billion).

DIVIDEND

The net profit for the year of KShs 21.8 million (2019: KShs 1,080.8 million) has been added to retained earnings. The directors do not recommend a dividend payment for the year ended 31 December 2020 (2019: Nil).

DIRECTORS

The directors who served during the year and up to the date of this report are set out on page 1.

DISCLOSURES TO AUDITORS

The directors confirm that with respect to each director at the time of approval of this report:

- (a) there was, as far as each director is aware, no relevant audit information of which the company's auditor is unaware; and
- (b) each director had taken all steps that ought to have been taken as a director so as to be aware of any relevant audit information and to establish that the company's auditor is aware of that information.

TERMS OF APPOINTMENT OF AUDITORS

The Auditor- General is responsible for the statutory audit of the consolidated and separate financial statements in accordance with Article 229 of the Constitution of Kenya. Section 23(1) of the Public Audit Act 2015, empowers the Auditor – General to nominate other auditors to carry out an audit on their behalf. KPMG Kenya who were appointed by the Auditor – General, have carried out the audit for the year ended 31 December 2020.

APPROVAL

The consolidated and separate financial statements were approved and authorised for issue by the board of directors on **15 March 2021**.

BY ORDER OF THE BOARD


Company Secretary

Date: 15 March 2021

The Directors are responsible for the preparation and presentation of the consolidated and separate financial statements of Development Bank of Kenya Limited (the "Group" and "Company") set out on pages 18 to 86 which comprise the consolidated and bank statements of financial position as at 31 December 2020, and the consolidated and bank statements of comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and the notes to the financial statements, including a summary of significant accounting policies and other explanatory information, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. The Directors are of the opinion that the financial statements give a true and fair view of the financial position and the profit or loss of the group and the company.

The Directors' responsibilities include: determining that the basis of accounting described in Note 2 is an acceptable basis for preparing and presenting the financial statements in the circumstances, preparation and presentation of financial statements in accordance with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015 and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

Under the Kenyan Companies Act, 2015, the Directors are required to prepare financial statements for each financial year which give a true and fair view of the financial position of the group and the company as at the end of the financial year and of the profit or loss of the group and the company for that year. It also requires the Directors to ensure the company keeps proper accounting records which disclose with reasonable accuracy the financial position and profit or loss of the group and the company.

The Directors 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 made an assessment of the company and group ability to continue as a going concern and have no reason to believe the group and company will not be a going concern for at least the next twelve months from the date of this statement.

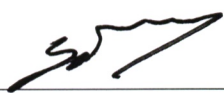
Approval of the consolidated and separate financial statements

The consolidated and separate financial statements, as indicated above, were approved and authorised for issue by the Board of Directors on **15 March 2021**.



Victor Kidiwa

Date: 15 march 2021



Sammy Chepkwony

Date: 15 March 2021



KPMG Kenya
Certified Public Accountants
8th Floor, ABC Towers
Waiyaki Way
P.O.Box 40612 00100 GPO
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DEVELOPMENT BANK OF KENYA LIMITED

REPORT OF THE AUTHORISED AUDITOR (APPOINTED UNDER SECTION 23(1) OF THE PUBLIC AUDIT ACT, NO. 34 OF 2015) TO THE AUDITOR-GENERAL

Report on the audit of the consolidated and separate financial statements

Opinion

We have audited the consolidated and separate financial statements of Development Bank of Kenya Limited (the “Group” and “Bank”) as set out on pages 18 to 86, which comprise the Consolidated and Bank statements of financial position as at 31 December 2020, and the Consolidated and Bank statements of comprehensive income, the Consolidated and Bank statements of changes in equity and the Consolidated and Bank statements of cash flows for the year then ended, and notes to the consolidated and separate financial statements, including a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated and separate financial statements give a true and fair view of the consolidated and separate financial position of Development Bank of Kenya Limited as at 31 December 2020, and of its consolidated and separate financial performance and its consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) and in the manner required by the Kenyan Companies Act, 2015.

Basis for opinion

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

Key audit matters

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



DEVELOPMENT BANK OF KENYA LIMITED

REPORT OF THE AUTHORISED AUDITOR (APPOINTED UNDER SECTION 23(1) OF THE PUBLIC AUDIT ACT, NO. 34 OF 2015) TO THE AUDITOR-GENERAL (CONTINUED)

Report on the audit of the consolidated and separate financial statements (Continued)

Key audit matters (continued)

Impairment allowances (expected credit losses) on loans and advances at amortised cost in the consolidated and separate financial statements	
<p>The disclosure associated with credit risk is set out in the financial statements in the following notes:</p> <ul style="list-style-type: none"> — Note 2 (e) – Impairment (page 32 – 34) — Note 4 (a) – Credit risk (page 40 – 54) — Note 19 – Impairment losses on loans and advances charged to profit or loss (page 72 – 73) 	
<i>The key audit matter</i>	<i>How the matter was addressed</i>
<p>Subjective estimate</p> <p>The estimation of expected credit losses (“ECL”) on loans and advances, involves significant judgement and estimates. The key areas where we identified greater levels of management judgement in the Group’s and Bank’s ECL assessment and therefore increased levels of audit focus are:</p> <ul style="list-style-type: none"> — Model estimations – inherently judgemental modelling is used to estimate ECL which involves determining probabilities of default (“PD”), loss given default (“LGD”), and exposures at default (“EAD”). The PD model is a key driver of complexity in the Group’s and Bank’s ECL modelling approach. — Significant increase in credit risk (“SICR”) – the criteria selected to identify a significant increase in credit risk is a key area of judgement within the Group’s and Bank’s ECL calculation as these criteria determine whether a 12 month or lifetime provision is recorded. — Economic scenarios – Financial instruments (IFRS 9) requires the Group and Bank to measure ECLs on a forward-looking basis reflecting a range of future economic conditions. Significant management judgment is applied to determining the forward-looking information in the economic scenarios used and the probability weightings applied to them especially when considering the current uncertain economic environment as a result of COVID-19. 	<p>Our procedures in this area included:</p> <ul style="list-style-type: none"> — Obtaining an understanding of the credit management processes and the key systems, applications and controls used in determination of the ECL and assessing the relevant general IT and applications controls. This included assessing the design and operating effectiveness of the key controls over the staging criteria and challenging the accuracy of the key inputs and assumptions into the IFRS 9 impairment models. This was performed by; <ul style="list-style-type: none"> ▪ Selecting a sample of outstanding loans from the Group’s and Bank’s loan book and evaluating whether significant facilities are correctly staged, classified and valued based on IFRS 9 principles as well as regulatory considerations; ▪ For a sample of key data inputs and assumptions applied in the determination of ECL assessing the accuracy of economic forecasts and challenging PD assumptions applied by involving our specialists in the reperformance of the economic forecasts and PDs; ▪ Evaluating the appropriateness of the Group’s and Bank’s assessment of the SICR criteria used by assessing the qualitative and quantitative factors used by management in their evaluation of the classification into stages 1, 2 and 3;



DEVELOPMENT BANK OF KENYA LIMITED

REPORT OF THE AUTHORISED AUDITOR (APPOINTED UNDER SECTION 23(1) OF THE PUBLIC AUDIT ACT, NO. 34 OF 2015) TO THE AUDITOR-GENERAL (CONTINUED)

Report on the audit of the consolidated and separate financial statements (Continued)

Key audit matters (continued)

Impairment allowances on loans and advances at amortised cost in the consolidated and separate financial statements – continued	
<i>The key audit matter</i>	<i>How the matter was addressed</i>
<p>We determined that the impairment on loans and advances to customers to be a key audit matter due to the high degree of estimation uncertainty and judgement applied by management in determination of ECL.</p>	<ul style="list-style-type: none"> ▪ Assessing the appropriateness of parameters used in the statistical models in respect of Probability of Default (PDs), Loss Given Default (LGDs), and Exposure at Default (EADs) by considering local economic conditions, and; ▪ Evaluating management’s basis for establishing stage 3 loss allowances in terms of the Group’s and Bank’s policies and in terms of the requirements of IFRS 9. This included challenging reasonability of management assumptions on cashflows projections and time to realization for a sample of the facilities. <p>— Making use of our internal financial risk modelling specialists to:</p> <ul style="list-style-type: none"> ▪ Assess the Group’s and Bank’s methodology for determining the economic scenarios used in the forward-looking information and the probability weightings applied to the scenarios. ▪ Assess the reasonableness of the Group’s and Bank’s adjustment to the macroeconomic overlay models to incorporate the impact of economic uncertainty.

Other matter

We draw attention to the fact that our responsibility is to report and express an opinion on the outcome of our audit of the consolidated and separate financial statements to the Auditor-General. The Auditor-General is responsible for reporting on his examination of these financial statements to the Cabinet Secretary responsible for the Group and Bank for presentation to the National Assembly.



DEVELOPMENT BANK OF KENYA LIMITED

REPORT OF THE AUTHORISED AUDITOR (APPOINTED UNDER SECTION 23(1) OF THE PUBLIC AUDIT ACT, NO. 34 OF 2015) TO THE AUDITOR-GENERAL (CONTINUED)

Report on the audit of the consolidated and separate financial statements (Continued)

Other information

The directors are responsible for the other information. The other information comprises the information included in the *Development Bank of Kenya Limited, Annual Report and Financial Statements for the year ended 31 December 2020*, but does not include the consolidated and separate financial statements and our auditor's report thereon.

Our opinion on the consolidated and separate financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated and separate financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Directors' responsibilities for the consolidated and separate financial statements

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

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

Authorised auditor's responsibilities for the audit of the consolidated and separate financial statements

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



DEVELOPMENT BANK OF KENYA LIMITED

REPORT OF THE AUTHORISED AUDITOR (APPOINTED UNDER SECTION 23(1) OF THE PUBLIC AUDIT ACT, NO. 34 OF 2015) TO THE AUDITOR-GENERAL (CONTINUED)

Report on the audit of the consolidated and separate financial statements (Continued)

Authorised auditor's responsibilities for the audit of the consolidated and separate financial statements (continued)

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

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

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

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



DEVELOPMENT BANK OF KENYA LIMITED

**REPORT OF THE AUTHORISED AUDITOR (APPOINTED UNDER SECTION 23(1) OF
THE PUBLIC AUDIT ACT, NO. 34 OF 2015) TO THE AUDITOR-GENERAL (CONTINUED)**

Report on other legal and regulatory requirements

As required by the Kenyan Companies Act, 2015, we report to you based on our audit, that in our opinion, the information given in the report of the directors on pages 9 and 10 is consistent with the consolidated and separate financial statements.

The signing partner responsible for the audit resulting in this independent auditor's report is CPA Jacob Gathecha – P/1610.

KPMG Kenya

**KPMG Kenya
Certified Public Accountants
PO Box 40612 – 00100
Nairobi**

Date: *29 March 2021*

REPUBLIC OF KENYA

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NAIROBI

REPORT OF THE AUDITOR-GENERAL ON DEVELOPMENT BANK OF KENYA LIMITED FOR THE YEAR ENDED 31 DECEMBER, 2020

REPORT ON THE FINANCIAL STATEMENTS

Opinion

The accompanying financial statements of Development Bank of Kenya Limited (the Group and Bank) set out on pages 18 to 86, which comprise the Consolidated and Bank statements of financial position as at 31 December, 2020, and the Consolidated and Bank statements of comprehensive income, Consolidated and Bank statements of changes in equity and the Consolidated and Bank statements 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 KPMG Kenya, auditors appointed under Section 23 of the Public Audit Act, 2015. 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.

In my opinion, the Consolidated and Bank financial statements present fairly, in all material respects, the financial position of Development Bank of Kenya Limited as at 31 December, 2020, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) and comply with the Kenya Companies Act, 2015 and the Banking Act, 2012.

Basis for Opinion

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Development Bank of Kenya Limited Management in accordance with ISSAI 130 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of Matter

Material Uncertainty Related to Going Concern

I draw attention to the statement of directors responsibilities where the Directors' have made an assessment of the Company and ability of the Group to continue as a going

concern and have no reason to believe the Group and Bank will not be a going concern for at least the next twelve months from the date of this statement.

During the year under review, the Bank made progress in improving its liquidity position to 22.4%, and 2.4 percentile above the Central Bank of Kenya (CBK) requirement of 20%. Further the Bank reported an improved performance by reporting profit from operating activities of Kshs.20,579,000 (Kshs.16,527,000 in 2019). However, the return on investment on the total asset base is negligible at 0.01% in comparison with the average Treasury Bill rate of 6.687% for the year.

Further, the Small Enterprises Finance Company Limited, a fully owned subsidiary of the Development Bank of Kenya Limited has ceased financing new development projects and is currently pursuing recovery of existing project loans and advances. The Company is dormant and also facing financial challenges with the increase in the level of non-performing loans and reduced interest margins which are adversely affecting its profitability.

My opinion is not modified in respect of this matter.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, are of most significance in the audit of the financial statements of the current year. These matters were addressed in the context of the audit of the financial statements as a whole, and in forming my opinion thereon, and I do not provide a separate opinion on these matters. For each matter below, a description of how the audit addressed the matter is provided in that context.

Impairment Allowances on Loans and Advances at Amortised Cost in the Consolidated and Bank Financial Statements	
The Key Audit Matter	How the matter was addressed
We determined that the impairment on loans and advances to customers to be a key audit matter due to the high degree of estimation uncertainty and significant judgement applied by Management in determination of Expected Credit Losses (ECL).	<ul style="list-style-type: none"> ▪ Assessing the appropriateness of parameters used in the statistical models in respect of Probability of Default (PDs), Loss Given Default (LGDs), and Exposure at Default (EADs) by considering local economic conditions, and; ▪ Evaluating Management's basis for establishing Stage 3 loss allowances in terms of the Group's and Bank's policies and in terms of the requirements of IFRS 9. This included challenging reasonability of Management assumptions on cashflow projections and time to

Impairment Allowances on Loans and Advances at Amortised Cost in the Consolidated and Bank Financial Statements

The Key Audit Matter	How the matter was addressed
	<p>realization for a sample of the facilities.</p> <ul style="list-style-type: none"> ▪ Making use of our internal financial risk modelling specialists to: ▪ Assess the Group's and Bank's methodology for determining the economic scenarios used in the forward-looking information and the probability weightings applied to the scenarios. ▪ Assess the key economic variables used in the determination of ECL, including agreeing a sample of economic variables to external sources, as well as the overall reasonableness of the economic forecasts by comparing the Group's and Banks' forecasts to reputable, external sources of macroeconomic forecasts.

Other Information

The Board of Directors is responsible for the other information. The other information comprises the information included in the annual report and financial statements, but does not include the consolidated and separate financial statements and my audit report thereon.

My opinion on the bank financial statements does not cover the other information and I do not express any form of assurance conclusion thereon.

In connection with my audit of the Consolidated and Bank financial statements, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Consolidated and Bank financial statements or my knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, except for the matter described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, I confirm that, nothing else has come to my attention to cause me to believe that internal controls, risk management and governance were not effective.

Basis for Conclusion

Corporate Governance Deficiencies

The Mwongozo Code guidelines on term limits for Board Members requires that no individual member should serve for a cumulative period exceeding six years. However, one Board Member of the Bank had exceeded the set limit. In the circumstance, the Bank is not in compliance with the Mwongozo Code on good governance.

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal control, risk management and governance were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Kenya Companies Act, 2015, I report based on my 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, adequate accounting records have been kept by the Bank, so far as appears from the examination of those records; and,
- iii. The Bank's financial statements are in agreement with the accounting records and returns.

Responsibilities of Management and the Board of Directors

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

In preparing the financial statements, Management is responsible for assessing Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidated the Bank or cease operations.

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

In addition to the responsibility for the preparation and presentation of the financial statements described above, Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public resources are applied in an effective way.

The Board of Directors is responsible for overseeing the Bank's financial reporting process, reviewing the effectiveness of how the Bank monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

Auditor-General's Responsibilities for the Audit

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high

level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

In addition to the audit of the financial statements, a compliance audit is planned and performed to express a conclusion about whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that govern them and that public resources are applied in an effective way, in accordance with the provisions of Article 229(6) of the Constitution and submit the audit report in compliance with Article 229(7) of the Constitution.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal control in order to give an assurance on the effectiveness of internal controls, risk management and overall governance processes and systems in accordance with the provisions of Section 7(1)(a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal control may not prevent or detect misstatements and instances of non-compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

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


- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.

- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Bank to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

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

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

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


Nancy Gathungu
AUDITOR-GENERAL

Nairobi

06 July, 2021

Consolidated statement of comprehensive income

	Note	2020 KShs'000	2019 KShs'000
Interest income	5	1,213,925	1,336,084
Interest expense	6	(848,821)	(928,800)
Net interest income		361,104	407,284
Net fees and commission income	7	22,231	15,881
Profit on sale of Finance House	8 (i)	-	1,062,588
Other operating income	8 (ii)	81,760	65,235
Operating income		469,095	1,550,988
Impairment losses on financial assets	19	(31,137)	(8,128)
Operating expenses	9	(417,417)	(403,668)
Profit before income tax	11	20,541	1,139,192
Income tax expense	12	1,289	(58,419)
Profit for the year		21,830	1,080,773
Other comprehensive income			
<i>Items that will not be reclassified to profit or loss:</i>			
Net change in fair value of available for sale financial assets	13	(156,168)	-
Deferred tax on fair value of available-for -sale financial assets	13	7,808	-
Other comprehensive income net of tax		(148,360)	-
Total comprehensive income		<u>(126,530)</u>	<u>1,080,773</u>
Earnings per share (KShs per share)	15	<u>0.42</u>	<u>20.73</u>
Dividends per share (KShs per share)	14	<u>-</u>	<u>-</u>

The notes set out on pages 26 to 86 form an integral part of these financial statements.



Bank statement of comprehensive income

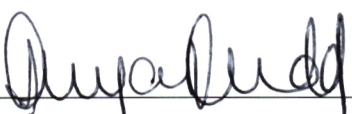
	Note	2020 KShs'000	2019 KShs'000
Interest income	5	1,211,690	1,333,849
Interest expense	6	(849,381)	(929,363)
Net interest income		362,309	404,486
Net fees and commission income	7	22,231	15,881
Profit on sale of Finance House	8 (i)	-	1,062,588
Other operating income	8 (ii)	81,760	64,985
Operating income		466,300	1,547,940
Impairment losses on financial assets	19	(30,779)	(8,138)
Operating expenses	9	(416,641)	(402,978)
Profit before income tax	11	18,880	1,136,824
Income tax expense	12	1,699	(57,709)
Profit for the year		20,579	1,079,115
<i>Items that may be reclassified to Profit or loss:</i>			
Net change in fair value of available for sale financial	13	(156,168)	-
Deferred tax on fair value of available-for -sale	13	7,808	-
Total other comprehensive income for the year		(148,360)	-
Total comprehensive income		(127,781)	1,079,115
Earnings per share (KShs per share)	15	0.39	20.70
Dividends per share (KShs per share)	14	-	-

The notes set out on pages 26 to 86 form an integral part of these financial statements.

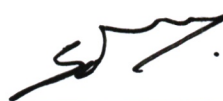
Consolidated statement of financial position

	Note	2020 KShs'000	2019 KShs'000
ASSETS			
Cash and balances with Central Bank of Kenya	16	682,875	361,419
Financial assets at fair value through profit and loss	17	103,177	101,767
Financial assets at amortised cost	17	3,952,870	4,553,553
Deposits and balances due from banking institutions	18	2,582,928	923,395
Loans and advances to customers	19	8,609,289	7,911,046
Other assets	23	174,274	226,096
Financial assets at fair value through other comprehensive income	20	669,245	825,413
Current income tax	22	29,927	30,057
Deferred income tax	24	111,378	101,841
Property and equipment	25	298,234	315,583
TOTAL ASSETS		<u>17,214,197</u>	<u>15,350,170</u>
LIABILITIES			
Deposits and balances due to banking institutions	26	2,077,535	939,205
Customer deposits	27	6,174,965	5,064,685
Borrowings	28	4,672,533	4,877,168
Lease liabilities	32(b)	156,018	183,146
Other liabilities	29	292,633	318,923
		<u>13,373,684</u>	<u>11,383,127</u>
EQUITY			
Share capital	30	1,042,500	1,042,500
Retained earnings		1,370,057	1,622,871
Statutory reserves	36 (a)	832,890	558,246
Other reserves	36 (b)	595,066	743,426
		<u>3,840,513</u>	<u>3,967,043</u>
TOTAL LIABILITIES AND EQUITY		<u>17,214,197</u>	<u>15,350,170</u>

The financial statements set out on pages 18 to 86 were approved and authorised for issue by the Board of Directors on 15 March 2021 and were signed on its behalf by:



 Victor Kidiwa



 Sammy Chepkwony

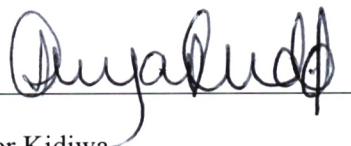
The notes set out on pages 26 to 86 form an integral part of these financial statements.



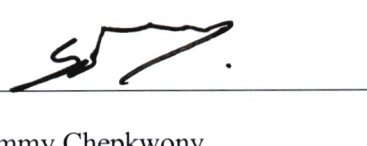
Bank statement of financial position

ASSETS	Note	2020 KShs'000	2019 KShs'000
Cash and balances with Central Bank of Kenya	16	682,875	361,419
Financial assets at fair value through profit and loss	17	103,177	101,767
Financial assets at amortised cost	17	3,931,826	4,532,494
Deposits and balances due from banking institutions	18	2,582,928	923,395
Loans and advances to customers	19	8,609,289	7,911,046
Other assets	23	174,274	226,095
Financial assets at fair value through other comprehensive income	20	669,245	825,413
Current income tax	22	27,119	27,119
Investment in subsidiary	21	32,048	32,048
Deferred income tax	24	111,197	101,690
Property and equipment	25	298,234	315,583
TOTAL ASSETS		<u>17,222,212</u>	<u>15,358,069</u>
LIABILITIES			
Deposits and balances due to banking institutions	26	2,077,535	939,205
Customers deposits	27	6,201,947	5,090,079
Borrowings	28	4,672,533	4,877,168
Lease liabilities	32(b)	156,018	183,146
Other liabilities	29	291,521	318,032
		<u>13,399,554</u>	<u>11,407,630</u>
EQUITY			
Share capital	30	1,042,500	1,042,500
Retained earnings		1,352,202	1,606,267
Statutory reserves	36 (a)	832,890	558,246
Other reserves	36 (b)	595,066	743,426
		<u>3,822,658</u>	<u>3,950,439</u>
TOTAL LIABILITIES AND EQUITY		<u>17,222,212</u>	<u>15,358,069</u>

The financial statements set out on pages 18 to 86 were approved and authorised for issue by the Board of Directors on 15 March 2021 and were signed on its behalf by:



Victor Kidiwa



Sammy Chepkwony

The notes set out on pages 26 to 86 form an integral part of these financial statements.

Consolidated statement of changes in equity

	Share capital	Statutory reserves	Other reserves	Retained earnings	Total
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
2019					
At 1 January 2019	1,042,500	349,913	743,426	750,431	2,886,270
Comprehensive income for the year					
Profit for the year	-	-	-	1,080,773	1,080,773
Transfer to statutory reserves		208,333	-	(208,333)	-
Total comprehensive income for the year	-	208,333	-	872,440	1,080,773
At 31 December 2019	1,042,500	558,246	743,426	1,622,871	3,967,043
2020					
At 1 January 2020	1,042,500	558,246	743,426	1,622,871	3,967,043
Comprehensive income for the year					
Profit for the year	-	-	-	21,830	21,830
Transfer to statutory reserves	-	274,644	-	(274,644)	-
Other comprehensive income for the year					
Changes in fair value	-	-	(148,360)	-	(148,360)
Total comprehensive income for the year	-	274,644	(148,360)	(252,814)	(126,530)
At 31 December 2020	1,042,500	832,890	595,066	1,370,057	3,840,513

The notes set out on pages 26 to 86 form an integral part of these financial statements.

Bank statement of changes in equity

	Share capital KShs'000	Statutory reserves KShs'000	Other reserves KShs'000	Retained earnings KShs'000	Total KShs'000
2019					
At 1 January 2019	1,042,500	349,913	743,426	735,485	2,871,324
Comprehensive income for the year					
Profit for the year	-	-	-	1,079,115	1,079,115
Transfer to statutory reserves	-	208,333	-	(208,333)	-
Total comprehensive income for the year	-	208,333	-	870,782	1,079,115
At 31 December 2019	1,042,500	558,246	743,426	1,606,267	3,950,439
2020					
At 1 January 2020	1,042,500	558,246	743,426	1,606,267	3,950,439
Comprehensive income for the year					
Profit for the year	-	-	-	20,579	20,579
Transfer to statutory reserves	-	274,644	-	(274,297)	-
Other comprehensive income for the year					
Changes in fair value	-	-	(148,360)	-	(148,360)
Total comprehensive income for the year	-	274,644	(148,360)	(253,065)	(127,781)
At 31 December 2020	1,042,500	832,890	595,066	1,352,202	3,822,658

The notes set out on pages 26 to 86 form an integral part of these financial statements.

Consolidated statement of cash flows

	Note	2020 KShs'000	2019 KShs'000
Operating activities			
Profit before taxation		20,541	1,139,192
Profit on sale of finance house		-	(1,062,588)
Depreciation	25	70,789	23,269
Interest on lease liabilities	32	19,390	20,553
Interest charged on borrowings		12,604	16,516
Interest paid on lease liabilities	32	(38,279)	(2,178)
Tax paid	22	(310)	(73,888)
Cash flows from operating activities before changes in operating assets and liabilities		84,735	60,876
Changes in operating assets and liabilities			
Loans to customers		(698,243)	475,651
Deposits held for regulatory purposes		26,079	(180,167)
Investments in treasury bonds		599,273	(25,458)
Deposits due from banks longer than 90 days		(327,982)	(26,213)
Other assets		51,822	42,406
Deposits due to banks longer than 90 days		177,052	-
Customer's deposits		1,110,280	(664,794)
Other liabilities (net of lease liabilities)		(26,290)	(270,873)
Net cash generated from operations		996,726	(588,572)
Cash flows from investing activities			
Purchase of property and equipment	25	(53,440)	(51,298)
Proceeds from sale of property		-	960,921
Net cash used in investing activities		(53,440)	909,623
Cash flows from financing activities			
Interest paid on borrowings		(12,604)	(16,516)
Lease principal payments		(8,239)	(588)
Loans receipts		500,000	-
Loans repayments		(704,635)	(160,297)
Net cash used in financing activities		(225,478)	(177,401)
Net increase in cash and cash equivalents		717,808	143,650
Cash and cash equivalents balances as at start of year		45,107	(98,543)
Cash and cash equivalents at end of year	31	762,915	45,107

The notes set out on pages 26 to 86 form an integral part of these financial statements.

Bank statement of cash flows

		2020	2019
	Note	KShs'000	KShs'000
Operating activities			
Profit before taxation		18,880	1,136,824
Profit on sale of finance house		-	(1,062,588)
Depreciation	25	70,789	23,269
Interest on lease liabilities	32	19,390	20,553
Interest charged on borrowings		12,604	16,516
Interest paid on lease liabilities	32	(38,279)	(2,178)
Tax paid	22	-	(73,579)
		<u>83,384</u>	<u>58,817</u>
Cash flows from operating activities before changes in operating assets and liabilities			
Changes in operating assets and liabilities			
Loans to customers		(698,243)	475,651
Deposits held for regulatory purposes		26,079	(180,167)
Investments in treasury bonds		599,258	(25,473)
Deposits from banks longer than 90 days		(327,982)	(26,213)
Other assets		51,821	42,407
Deposits due to other banks longer than 90 days		177,052	-
Customer's deposits		1,111,868	(662,421)
Other liabilities		(26,511)	(271,173)
		<u>996,726</u>	<u>(588,572)</u>
Net cash generated from operations			
Cash flows from investing activities			
Purchase of property and equipment	25	(53,440)	(51,298)
Proceeds from sale of property		-	960,921
		<u>(53,440)</u>	<u>909,623</u>
Net cash used in investing activities			
Cash flows from financing activities			
Interest paid on loan capital		(12,604)	(16,516)
Lease principal payments		(8,239)	(588)
Loans received		500,000	-
Loans repaid		(704,635)	(160,297)
		<u>(225,478)</u>	<u>(177,401)</u>
Net cash used in financing activities			
Net increase in cash and cash equivalents			
Cash and cash equivalents as at start of year		717,808	143,650
		<u>45,107</u>	<u>(98,543)</u>
Cash and cash equivalents at end of year	31	<u>762,915</u>	<u>45,107</u>

The notes set out on pages 26 to 86 form an integral part of these financial statements.

Notes to the financial statements

1. General information

Development Bank of Kenya Limited (the “Group”, “Bank” or the “Company”) is incorporated as a limited company in Kenya under the Kenyan Companies Act, and is domiciled in Kenya. The address of its registered office is as follows:

Finance House
Loita Street
PO Box 30483, 00100
Nairobi

The annual financial statements have been prepared in accordance with International Financial Reporting Standards and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) of the International Accounting Standards Board (IASB) and the requirements of the Kenyan Companies Act, 2015. Reference to financial statements includes consolidated and separate financial statements.

For the Kenyan Companies Act, 2015 reporting purposes, the balance sheet is represented by the statement of financial position and profit and loss account by the statement of comprehensive income in these financial statements.

The consolidated and separate financial statements are prepared in millions of Kenya Shillings (Shs ‘million), the functional currency of the group. All amounts have been rounded to the nearest thousand (Kshs’ 000) except when otherwise indicated.

2. Summary of significant accounting policies

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

(a) Basis of preparation

Changes in accounting policies and disclosures

(i) *New standards, amendments and interpretations effective and adopted during the year*

During the current year, the bank has adopted all of the new and revised standards and interpretations issued by the IASB and IFRIC that are relevant to its operations and effective for the annual periods beginning on 1 January 2020. The impact of the adoption of these new and revised standards and interpretations has been documented below:

New standard or amendments	Effective for annual periods beginning on or after
— Amendments to References to Conceptual Framework in IFRS Standards	1 January 2020
— Definition of a Business (Amendments to IFRS 3)	1 January 2020
— Definition of Material (Amendments to IAS 1 and IAS 8)	1 January 2020

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(a) Basis of preparation (continued)

Changes in accounting policies and disclosures (continued)

(i) New standards, amendments and interpretations effective and adopted during the year - continued

New standard or amendments	Effective for annual periods beginning on or after
— Interest Rate Benchmark Reform (Amendments to IFRS 9, IAS 39 and IFRS 7)	1 January 2020
— Extension of the Temporary Exemption from Applying IFRS 9 (Amendments to IFRS 4)	1 January 2020
— COVID-19-Related Rent Concessions (Amendment to IFRS 16)	1 June 2020

These standards did not have a material impact on the financial statements of the Group and Bank.

(ii) New standards, amendments and interpretations in issue but not yet effective for the year ended 31 December 2020

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2020, and have not been applied in preparing these financial statements.

The Group does not plan to adopt these standards early. These are summarised below:

New standards or amendments	Effective for annual period beginning or after
— Interest Rate Benchmark Reform Phase 2	1 January 2021
— Onerous Contracts Cost of Fulfilling a Contract 01 Jan 2022 (Amendments to IAS 37)	1 January 2022
— Annual Improvements to IFRS Standards 2018-2020	1 January 2022
— Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)	1 January 2022
— Reference to the Conceptual Framework (Amendments to IFRS 3)	1 January 2022
— IFRS 17 Insurance Contracts	1 January 2023
— Classification of liabilities as current or non-current (Amendments to IAS 1)	1 January 2023
— Amendments to IFRS 17	1 January 2023
— Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)	Optional and effective date deferred indefinitely

All standards and interpretations will be adopted at their effective date (except for those standards and interpretations that are not applicable to the Group and Bank).

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(b) Consolidation principles

The consolidated financial statements include the financial statements of Development Bank of Kenya Limited (DBK) and its wholly owned subsidiary company, Small Enterprises Finance Company Limited (SEFCO), which is controlled by the bank. Control exists when the bank has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. All inter-company balances and transactions have been eliminated on consolidation.

(c) Foreign currency translation

(i) Functional and Presentation Currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which entity operates ('the Functional Currency'). The consolidated financial statements are presented in Kenya shillings, which is the Group's functional currency. All financial information presented in these consolidated financial statements has been rounded off to the nearest thousand Kenya shillings

(ii) Transactions and balances

Foreign currency transactions are translated into the Functional Currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. 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 in the income statement, except when deferred in other comprehensive income as qualifying cash flow hedges and qualifying net investment hedges. Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in the income statement within "finance income or costs". All other foreign exchange gains and losses are presented in the statement of profit or loss for the year within "other gains/losses-net".

Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortised cost are recognised in profit or loss, and other changes in carrying amount are recognised in other comprehensive income.

(d) Revenue recognition

Income is recognised on an accrual basis.

(i) Interest income

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for Purchased or originated credit impaired ('POCI') financial assets and Financial assets that are not "POCI" but have subsequently become credit impaired. For Purchased or originated credit-impaired ('POCI') financial assets the original credit-adjusted effective interest rate is applied to the amortised cost of the financial asset.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(d) Revenue recognition (continued)

(i) Interest income - continued

Financial assets that are not 'POCI' but have subsequently become credit-impaired (or 'stage 3'), interest revenue is calculated by applying the effective interest rate to their amortised cost (i.e. net of the expected credit loss provision).

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

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset. For 'POCI' financial assets if any — assets that are credit-impaired at initial recognition — the Group calculates the credit-adjusted effective interest rate, which is calculated based on the amortised cost of the financial asset instead of its gross carrying amount and incorporates the impact of expected credit losses in estimated future cash flows.

(ii) Fees and commission income

Fees and commission income that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including account servicing fees, investment are recognised as the related services are performed.

(iii) Dividend income

Dividend income is recognised once the right to receive the dividends has been established.

(e) Financial assets

(i) Measurement methods

Amortised cost and effective interest rate

The amortised cost is the amount at which the financial asset is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

When the Group revises the estimates of future cash flows, the carrying amount of the respective financial assets is adjusted to reflect the new estimate discounted using the original effective interest rate. Any changes are recognised in profit or loss.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(e) Financial assets (continued)

(i) *Measurement methods - continued*

Initial recognition and measurement

Financial assets are recognised when the entity becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the Group commits to purchase or sell the asset.

At initial recognition, the Group measures a financial asset at its fair value plus or minus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset, such as fees and commissions. Transaction costs of financial assets carried at fair value through profit or loss are expensed in profit or loss. Immediately after initial recognition, an expected credit loss allowance (ECL) is recognised for financial assets measured at amortised cost, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

When the fair value of financial assets differs from the transaction price on initial recognition, the group recognises the difference as follows:

When the fair value is evidenced by a quoted price in an active market for an identical asset (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.

In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

(ii) *Classification and subsequent measurement*

From 1 January 2018, the Group applied IFRS 9 and classifies its financial assets in the following measurement categories:

- (a) Fair value through profit or loss (FVPL);
- (b) Fair value through other comprehensive income (FVOCI); or
- (c) Amortised cost.

The classification requirements for debt and equity instruments are described below:

Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(e) Financial assets (continued)

(ii) *Classification and subsequent measurement - continued*

Debt instruments – continued

Classification and subsequent measurement of debt instruments depend on:

- (a) The Group's business model for managing the asset; and
- (b) the cash flow characteristics of the asset.

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

Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI'), and that are not designated at FVPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any expected credit loss allowance recognised and measured as described under the expected credit loss measurement section. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method. Financial assets classified in this category include treasury bills and treasury bonds purchased from the secondary market; loans and advances to banks and customers with fixed or determinate payment that are not quoted in active market.

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

Fair value through profit or loss: Assets that do not meet the criteria for amortised cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognised in profit or loss and presented in the profit or loss statement within 'Net trading income' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Net investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method. Financial instruments reclassified in this category are those that the Group holds principally for the purpose of short-term profit taking. These comprise mainly certain Treasury bonds.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(e) Financial assets (continued)

(ii) *Classification and subsequent measurement - continued*

Debt instruments – continued

Business model: the business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'other' business model and measured at FVPL. Factors considered by the Group in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Group assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement.

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

Equity instruments

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

The Group has designated at FVOCI investments in a small portfolio of equity securities. The Group chose this presentation alternative because the investments were made for strategic purposes rather than with a view to profit on a subsequent sale, and there are no plans to dispose of these investments in the short or medium term. There was no dividend recognised during the period nor transfers of the cumulative gain within equity.

(iii) *Impairment*

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

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(e) Financial assets (continued)

(iii) *Impairment - continued*

The measurement of ECL reflects:

- (a) An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- (b) The time value of money; and
- (c) Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

(iv) *Modification of loans*

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

- (a) If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- (b) Whether any substantial new terms are introduced that substantially affects the risk profile of the loan.
- (c) Significant extension of the loan term when the borrower is not in financial difficulty.
- (d) Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Group derecognises the original financial asset and recognises a 'new' asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Group also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit or loss as a gain or loss on derecognition.

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

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(e) Financial assets (continued)

(v) *Derecognition other than on a modification*

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

(f) Leases

At inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Bank uses the definition of a lease in IFRS 16.

The Group recognises a right-of-use asset and a lease liability from the date of initial application of IFRS 16 or at the lease commencement date for contracts after the date of initial application. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain re-measurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the profit rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, the Bank uses its incremental borrowing rate as the discount rate. The Bank determines the incremental borrowing rate as the rate of external borrowing that would be applicable to access funding to acquire the right-of-use assets.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments;
- variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Bank is reasonably certain to exercise, lease payments in an optional renewal period if the Bank is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Bank is reasonably certain not to terminate early.

The lease liability is measured at amortised cost using the effective profit rate method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, if the Bank changes its assessment of whether it will exercise an extension or termination option or if there is a revised in-substance fixed lease payment.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(f) Leases (continued)

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The Bank presents right-of-use assets in 'property and equipment' and lease liabilities in 'other liabilities' in the statement of financial position.

Short-term leases and leases of low-value assets

The Bank has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

(g) Property and equipment

All property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

— Buildings on leasehold land	over the lease period
— Furniture and equipment	8 years
— Computers	3 years
— Motor vehicles	4 years
— Leasehold improvements	6 years
— Right of Use Assets	Lease Term

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'Other (losses)/gains – net' in the income statement.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(h) Income tax

(i) Current income tax

The tax expense for the period comprises current and deferred income tax. Tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity respectively.

The current income tax charge is calculated on the basis of tax laws enacted or substantively enacted at the reporting date. The directors periodically evaluate positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. They establish provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

(ii) Deferred income tax

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill; deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current income tax assets against current income tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same entity or different taxable entities where there is an intention to settle the balances on a net basis.

(i) Employee benefits

(i) Post-employment benefits

The majority of the Group's employees are eligible for retirement benefits under a defined contribution plan.

Obligations for contributions to the defined contribution plan are recognised as an expense in profit or loss as incurred. Any difference between the charge to profit or loss income and the contributions payable is recorded in the statement of financial position under other assets or liabilities.

(ii) Leave

All employees are entitled to such leave as is determined by the Bank from time to time. All annual leave must be taken in the year it is earned subject to a maximum of 15 days carried forward. The bank does not compensate staff leave days carried forward in excess of 15 days unless sanctioned and supported by the head of department.

Leave days not taken within policy are accrued for at the individual staff salary scale.

Notes to the financial statements (Continued)

2. Summary of significant accounting policies (Continued)

(j) Cash and cash equivalents

For the purpose of presentation of the cash flows in the financial statements the cash and cash equivalents include cash and balances with Central Bank of Kenya net of cash ratio reserve, net balances from banking institutions, uncleared effects and investment in government securities with a maturity of three months or less from the date of acquisition.

(k) Dividends

Dividends are recognised as a liability in the period in which they are declared. Proposed dividends are disclosed as a separate component of equity.

(l) Provisions

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

(m) Non-financial guarantee contracts, letters of credit, performance bonds and loan commitments

Letters of credit, acceptances, guarantees and performance bonds, which are credit-related instruments, are generally given by the Group to support performance by a customer to third parties. Non-financial guarantees are those issued by the Group to a client to guarantee full and due performance of a contractor according to plans and specifications in a contract. If the contractor fails to perform under the contract, the Group will compensate the customer for losses incurred as a result and will then recoup the amount paid from the contractor.

Loan commitments provided by the Group are measured as the amount of the loss allowance. The Group has not provided any commitment that can be settled net in cash or by delivering or issuing another financial instrument. For loan commitments, the loss allowance is recognised as a provision.

3. Critical accounting estimates and judgements

In preparing these consolidated financial statements, management has made judgements and estimates that affect the application of the Group's accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are continuously reviewed on an ongoing basis are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances. Revisions to estimates are recognised prospectively.

This note provides an overview of the areas that involve a higher degree of judgement or complexity, and major sources of estimation uncertainty that have a significant risk of resulting in a material adjustment within the next financial year.

Notes to the financial statements (Continued)

3. Critical accounting estimates and judgements (Continued)

(a) Measurement of the expected credit allowance

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

Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is further detailed in Note 4(a), which also sets out key sensitivities of the ECL to changes in these elements.

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

- (i) Determining criteria for significant increase in credit risk;
- (ii) Choosing appropriate models and assumptions for the measurement of ECL;
- (iii) Establishing the number and relative weightings of forward-looking scenarios for each type of product and the associated ECL; and
- (iv) Establishing groups of similar financial assets for the purposes of measuring ECL.

Detailed information about the judgements and estimates made by the Group in the above areas is set out in Note 4(a).

(b) Income taxes

The Company is subject to income taxes in Kenya. Significant judgment is required in determining the Group's provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(c) Fair value of financial instruments

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

All financial instruments are initially recognised at fair value, which is normally the transaction price. In certain circumstances, the initial fair value may be based on a valuation technique which may lead to the recognition of profits or losses at the time of initial recognition. However, these profits or losses can only be recognised when the valuation technique used is based solely on observable market inputs.

Subsequent to initial recognition, some of the Group's financial instruments are carried at fair value, with changes in fair value either reported within the statement of comprehensive income or within other comprehensive income until the instrument is sold or becomes impaired. Details of the type and classification of the Group's financial instruments are set out in Note 4 and the accounting policy set out in Note 2 to the financial statements.

Notes to the financial statements (Continued)

3. Critical accounting estimates and judgements (Continued)

(c) Fair value of financial instruments (continued)

The fair values of quoted financial instruments in active markets are based on current prices. If the market for a financial instrument is not active, and for unlisted securities, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Where representative prices are unreliable because of illiquid markets, the determination of fair value may require estimation of certain parameters, which are calibrated against industry standards and observable market data, or the use of valuation models that are based on observable market data.

The fair value for the majority of the Group's financial instruments is based on observable market prices or derived from observable market parameters.

Equity investments that do not have an observable market prices are fair valued by applying various valuation techniques, such as earnings multiples, net assets multiples, discounted cash flows, and industry valuation benchmarks. These techniques are generally applied prior to any initial public offering after which an observable market price becomes available. Disposal of such investments are generally by market trades or private sales.

(d) Coronavirus (Covid-19) pandemic

The Covid-19 pandemic and its effects on the global and local economy have impacted our operations, customers and the financial performance. Various governments and regulators responded in unprecedented ways to protect the health of their communities, while regulators introduced measures to protect the financial system. The pandemic has therefore increased the estimation uncertainty in the preparation of these financial statements including;

- The extent and duration of the disruption to business arising from the actions of governments, business and consumers to contain the spread of the virus;
- The effectiveness of the government and Central Bank of Kenya measures to support businesses and consumers through the disruption and economic downturn; and
- The extent and duration of the expected economic downturn and subsequent recovery. This includes impacts on credit quality, liquidity, capital markets, increasing unemployment, decline in, consumer spending, reduction in economic activities and other restricting activities.

The Bank has made various estimates for future events in the financial statements based on forecasts of economic conditions which reflect expectations and assumptions as at 31 December 2020 and which the Bank believes are reasonable under the circumstances. There is a considerable degree of judgement involved in preparing these estimates. The underlying assumptions are also subject to uncertainties which are often outside the control of the Bank. Accordingly, actual economic conditions are likely to be different from those forecast since anticipated events do not occur as expected, and the effect of those differences may significantly impact accounting estimates included in the financial statements.

The significant accounting estimates impacted by these forecasts and associated uncertainties and largely related to expected credit losses, fair value measurement and the recoverable amount of non-financial assets. The impact of the Covid-19 pandemic on each of these estimates is included in the relevant notes to the financial statements.

Notes to the financial statements (Continued)

4. Financial risk management

Introduction and overview

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

- (a) Credit risk;
- (b) Liquidity risk; and
- (c) Market risks, comprising of interest rate risk, currency risk and price risk

Group's risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established the Asset and Liability (ALCO), Credit and Risk and Debt collection committees, which are responsible for developing and monitoring the Group's risk management policies in their specified areas. All Board committees have both executive and non-executive members and report regularly to the main Board on their activities.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Group Board Audit Committee is responsible for monitoring compliance with the Group's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Group. The Group Board Audit Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

(a) Credit risk

Credit risk is the risk of suffering financial loss, should any of the Group's customers, clients or market counterparties fail to fulfil their contractual obligations to the Group. Credit risk arises mainly from interbank, customer loans and advances, and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as financial guarantees and letters of credit.

The Group is also exposed to other credit risks arising from investments in debt securities and other exposures arising from its trading activities ('trading exposures') including non-equity trading portfolio assets. For risk management reporting purposes, the Group considers and consolidates all elements of credit risk exposure. Further, credit risk arising on trading securities is managed independently, but reported as a component of market risk exposure.

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Coronavirus (Covid-19) pandemic

As part of the credit risk management processes, the bank has restructured various facilities with customers in order to support them navigate through the economic disruptions. The restructure of facilities includes extension of repayments and moratorium for certain periods. The bank has also incorporated the government's directives on the pandemic in providing relief to customers and other measures put in place by the Central Bank of Kenya.

The Bank has also aligned the grouping of customers' financing arrangements based on economic sector which better represents the credit risk characteristics from the previous grouping based on customers' business segments. ECL has therefore been computed based on the economic sector grouping of financing arrangements with customers.

In determining when a significant increase in credit risk has occurred the bank uses quantitative test based on movement in PD, qualitative indicators, and a backstop of 30 days past due for all financing arrangements. For facilities subject to the Covid-19 restructure and modifications, an assessment of the significant increase in credit risk has been determined based on various measures of the customer's current financial position and earnings capacity as well as the qualitative and quantitative considerations.

Management of credit risk

Credit risk is the single largest risk for the Group's business; management therefore carefully manages its exposure to credit risk. The Board of Directors has delegated responsibility for the management of credit risk to its Board Credit Committee. The Board Credit Committee is responsible for oversight of the Group's credit risk, including:

- (i) 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;
- (ii) Establishing the authorisation structure for the approval and renewal of credit facilities;
- (iii) Reviewing and assessing credit risk. Group credit assesses all credit exposures in excess of designated limits, prior to facilities being committed to customers by the business unit concerned. Renewals and reviews of facilities are subject to the same review process;
- (iv) Limiting concentrations of exposure to counterparties and industries for loans and advances;
- (v) Developing and maintaining the Group'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 five grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. The responsibility for setting risk grades lies with the final approving executive / committee as appropriate. Risk grades are subject to regular reviews by Group Risk;

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Management of credit risk - continued

- (vi) Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports are provided to Group Credit on the credit quality of local portfolios and appropriate corrective action is taken; and
- (vii) Providing advice, guidance and specialist skills to business units to promote best practice throughout the Group in the management of credit risk. Each business unit is required to implement Group credit policies and procedures, with credit approval authorities delegated from the Group Credit Committee.

Credit risk measurement

Loans and advances (including loan commitments and guarantees)

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD). This is similar to the approach used for the purposes of measuring Expected Credit Loss (ECL) under IFRS 9.

Credit risk grading

The Group uses credit risk grading that reflect its assessment of the probability of default and specific characteristics of individual counterparties. Various qualitative and quantitative factors such as the facility arrears status, facility restructures as well as specific industry risk assessment are considered. In addition, the credit grading enable expert judgement from the credit risk team to be fed into the final internal credit rating for each exposure. This allows for considerations which may not be captured as part of the other data inputs into the model.

Expected credit loss measurement

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

- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Group.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'.



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Expected credit loss measurement - continued

- Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis. A description of inputs, assumptions and estimation techniques used in measuring the ECL is provided in this note.
- A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward-looking information.
- Purchased or originated credit-impaired financial assets are those financial assets that are credit-impaired on initial recognition. Their ECL is always measured on a lifetime basis (Stage 3).

Significant increase in credit risk (SICR)

The Group considers a financial instrument to have experienced a significant increase in credit risk based on its assessment of both quantitative factors and qualitative factors or when the backstop criteria have been met.

Quantitative criteria: This considers the facilities arrears status and considers whether expected contractual payments are 30 days past due.

Qualitative criteria: This considers whether the facility has been restructured due to cash flow difficulties experienced by the customer as well as an assessment of perceived risk of the industry in which the facility falls in. Further the group assesses the perceived risk of the obligor in assessment of financial instrument to have experienced a significant increase in credit risk.

The assessment of SICR incorporates forward-looking information. The criteria used to identify SICR are monitored and reviewed periodically for appropriateness by the independent Credit Risk team. A backstop is applied and the financial instrument considered to have experienced a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payments.

The Group has not used the low credit risk exemption for any financial instruments in the year ended 31 December 2020.

Definition of default and credit-impaired assets:

The Group defines a financial instrument as in default when the borrower is more than 90 days past due on its contractual payments. The definition has been used consistently across all ECL inputs i.e. PD, EAD and LGD. The criteria above have been applied to all financial instruments held by the Group and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD) and Loss given Default (LGD) throughout the Group's expected loss calculations.



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Significant increase in credit risk (SICR) - continued

Measuring ECL — Explanation of inputs, assumptions and estimation techniques:

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation (as per "Definition of default), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation.
- EAD is based on the amounts the Group expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD).
- Loss Given Default (LGD) represents the Group's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type of claim and availability of collateral or other credit support. LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the approximation of the original effective interest rate.

The Lifetime PD is developed by applying a maturity profile to the current 12M PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and credit grade band. This is supported by historical analysis.

The 12-month and lifetime EADs are determined based on the expected payment profile. The 12-month and lifetime LGDs are determined based on the factors which impact the recoveries made post default. These vary by product type. The Group has based on the entity's historical experience, determined the time to realization. Forced sale values of the land and non-land collateral are also used in the determination of the LGD. In some cases, the group determines the forced sale value assumption taking into account factors such as the most recent revaluation reports on the collateral, the perceived risk of the client whose assets are secured by a negative pledges, any other claims on collateral in instances where the Bank's claim ranks pari passu to that of other lenders and the exposure of all of a client's facilities where a single client has multiple facilities secured by the same collateral.



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Significant increase in credit risk (SICR) - continued

Measuring ECL — Explanation of inputs, assumptions and estimation techniques: - continued

Forward-looking economic information is also included in determining the 12-month and lifetime PD, EAD and LGD. The assumptions underlying the ECL calculation such as how the maturity profile of the PDs and how collateral values change etc are monitored and on an ongoing basis. There have been no significant changes in estimation techniques or significant assumptions made during the reporting period.

The group reviews all inputs, assumptions and estimation techniques applied in measuring the ECL to assess any changes and appropriateness on an annual basis. Consideration is made to changes in the business, changes in the economy, changes in the factors affecting the PD, LGD, EAD and other inputs. Such changes are expected to be very infrequent. There have been no significant changes in estimation techniques or significant assumptions made during the reporting period. Unless significant changes are identified, the Group expects to update the PDs, LGD and any other significant assumptions after every 3 years.

Forward-looking information incorporated in the ECL models

The assessment of SICR and the calculation of ECL both incorporate forward-looking information using macro-economic overlays. Overlays were estimated and applied for three different scenarios, base case scenario, downside scenario and optimistic scenario. These macroeconomic overlays and the probability of each economic scenario occurring were set using management judgement based on the assessment of the Group's portfolio performance. The number of scenarios and their attributes are reassessed at each reporting date. At 1 January 2018, 31 December 2019 and 31 December 2020, for all portfolios the Group concluded that three scenarios appropriately captured non-linearities.

The assessment of SICR is performed using the Lifetime PD under each of the base, and the other scenarios, multiplied by the associated scenario weighting, along with qualitative and backstop indicators. Following this assessment, the Group measures ECL as either a probability weighted 12 month ECL (Stage 1), or a probability weighted lifetime ECL (Stages 2 and 3). As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The Group considers these forecasts to represent its best estimate of the possible outcomes and has established that the chosen scenarios are appropriately representative of the range of possible scenarios.

Grouping of instruments for losses measured on a collective basis.

For expected credit loss provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous. In performing this grouping, there must be sufficient information for the group to be statistically credible. The appropriateness of groupings is monitored and reviewed on a periodic basis by the Credit Risk team.



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Significant increase in credit risk (SICR) - continued

Maximum exposure to credit risk — Financial instruments subject to impairment.

The following table contains an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets.



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

The following table contains an analysis of the credit risk exposure (credit quality analysis) of financial instruments for which an ECL allowance is recognised.

The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets.

Group	31-Dec-20			Total KShs'000	31-Dec-19
	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000		Total KShs'000
Cash and balances with Central Bank of Kenya	682,875	-	-	682,875	361,419
Financial assets at fair value through profit and loss	103,177	-	-	103,177	101,767
Financial assets at fair value through other comprehensive income	3,952,870	-	-	3,952,870	4,553,553
Deposits and balances due from banking institutions	2,582,928	-	-	2,582,928	923,395
Loans and advances to customers	3,795,155	2,565,843	3,828,076	10,189,074	9,409,288
Undrawn loan commitments	254,716	-	-	254,716	175,753
Other financial assets	153,761	-	-	153,761	209,390
Letters of credit and guarantees	966,362	-	-	966,362	774,604
Gross carrying amount	12,491,844	2,565,843	3,828,076	18,885,763	16,509,169
Impairment losses on financial assets	(139,564)	(249,548)	(1,190,673)	(1,579,785)	(1,498,242)
Net carrying amount	12,352,280	2,316,295	2,637,403	17,305,978	15,010,927



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Bank	31-Dec-20			Total KShs'000	31-Dec-19 Total KShs'000
	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000		
Cash and balances with central Bank of Kenya	682,875	-	-	682,875	361,419
Financial assets at fair value through profit and loss	103,177	-	-	103,177	101,767
Financial assets at fair value through other comprehensive income	3,931,826	-	-	3,931,826	4,532,494
Deposits and balances due from banking institutions	2,582,928	-	-	2,582,928	923,395
Loans and advances to customers	3,795,155	2,565,843	3,772,077	10,133,075	9,353,192
Undrawn loan commitments	254,716	-	-	254,716	175,753
Other financial assets	153,761	-	-	153,761	209,390
Letters of credit and guarantees	966,362	-	-	966,362	774,604
Gross carrying amount	12,470,800	2,565,843	3,772,077	18,808,720	16,432,014
Impairment losses on financial assets	(139,564)	(249,548)	(1,134,674)	(1,523,786)	(1,442,146)
Net carrying amount	12,331,236	2,316,295	2,637,403	17,284,934	14,989,868



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

The movement in the allowance for impairment for debt securities at amortised cost during the year was as follows (see Note 19 for the movement for the year ended 31 December 2020):

Group	31-Dec-20			Total KShs'000
	Stage 1 12 month ECL KShs'000	Stage 2 Lifetime ECL KShs'000	Stage 3 Lifetime ECL KShs'000	
Loans and advances at amortised cost				
Balances at 1 January	66,082	339,535	1,092,625	1,498,242
Transfer to Stage 1 (12 month ECL)	(29,364)	4,911	24,453	-
Transfer to Stage 2 (lifetime ECL not credit impaired)	35,710	(50,322)	14,612	-
Transfer to Stage 3 (lifetime ECL credit impaired)	117	10,435	(10,552)	-
Net remeasurement of loss allowances	59,490	(53,010)	149,994	156,474
New financial assets originated or purchased	5,740	1,532	-	7,272
Financial assets derecognised	(924)	(1,317)	(14,778)	(17,019)
Write offs	-	-	-	-
Recoveries from write offs	-	-	(65,184)	(65,184)
Balance at 31 December	136,851	251,764	1,191,170	1,579,785
Bank				
Loans and advances at amortised cost				
Balances at 1 January	66,082	339,535	1,036,529	1,442,146
Transfer to Stage 1 (12 month ECL)	(29,364)	4,911	24,453	-
Transfer to Stage 2 (lifetime ECL not credit impaired)	35,710	(50,322)	14,612	-
Transfer to Stage 3 (lifetime ECL credit impaired)	117	10,435	(10,552)	-
Net remeasurement of loss allowances	59,490	(53,010)	149,524	156,004
New financial assets originated or purchased	5,740	1,532	-	7,272
Financial assets derecognised	(924)	(1,317)	(14,261)	(16,502)
Write offs	-	-	-	-
Recoveries from write offs	-	-	(65,134)	(65,134)
Balance at 31 December	136,851	251,764	1,135,171	1,523,786

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Group	31-Dec-19			Total KShs'000
	Stage 1 12 month ECL KShs'000	Stage 2 Lifetime ECL KShs'000	Stage 3 Lifetime ECL KShs'000	
Loans and advances at amortised cost				
Balances at 1 January	46,459	406,814	1,022,769	1,476,042
Transfer to Stage 1 (12 month ECL)	(17,232)	16,981	251	-
Transfer to Stage 2 (lifetime ECL not credit impaired)	4,700	(69,108)	64,408	-
Transfer to Stage 3 (lifetime ECL credit impaired)	32,872	171,388	(204,260)	-
Net remeasurement of loss allowances	(1,400)	(202,275)	381,860	178,185
New financial assets originated or purchased	4,662	33,647	-	38,309
Financial assets derecognised	(3,979)	(17,912)	(19,798)	(41,689)
Write offs	-	-	-	-
Recoveries from write offs	-	-	(152,605)	(152,605)
Balance at 31 December	66,082	339,535	1,092,625	1,498,242
Bank				
Loans and advances at amortised cost				
Balances at 1 January	46,459	406,814	966,895	1,420,168
Transfer to Stage 1 (12 month ECL)	(17,232)	16,981	251	-
Transfer to Stage 2 (lifetime ECL not credit impaired)	4,700	(69,108)	64,408	-
Transfer to Stage 3 (lifetime ECL credit impaired)	32,872	171,388	(204,260)	-
Net remeasurement of loss allowances	(1,400)	(202,275)	381,860	178,185
New financial assets originated or purchased	4,662	33,647	-	38,309
Financial assets derecognised	(3,979)	(17,912)	(20,020)	(41,911)
Write offs	-	-	-	-
Recoveries from write offs	-	-	(152,605)	(152,605)
Balance at 31 December	66,082	339,535	1,036,529	1,442,146

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Collateral and other credit enhancements

The Group employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation. The Group prepares a valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically.

The Group holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to banks, except when securities are held as part of reverse repurchase and securities borrowing activity. Collateral held as security for financial assets other than loans and advances depends on the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured. Collateral is usually not held against investment securities, and no such collateral was held at 31 December 2020 or 2019.

The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period. The Group closely monitors collateral held for financial assets, as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

The Group closely monitors collateral held for financial assets, as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses.

Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

Loans and advances to customers	2020			Fair value of collateral held
	Gross exposure	Impairment allowance	Carrying amount	
Group	KShs'000	KShs'000	KShs'000	KShs'000
Carrying amount	10,189,074	1,579,785	8,609,289	18,326,779
Bank				Fair value of collateral held
	Gross exposure	Impairment allowance	Carrying amount	KShs'000
	KShs'000	KShs'000	KShs'000	KShs'000
Carrying amount	10,133,075	1,523,786	8,609,289	18,326,779

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Collateral and other credit enhancements - continued

Loans and advances to customers		2019		
Group	Gross exposure KShs'000	Impairment allowance KShs'000	Carrying amount KShs'000	Fair value of collateral held KShs'000
Carrying amount	9,409,288	(1,498,242)	7,911,046	24,803,562
Bank	Gross exposure KShs'000	Impairment allowance KShs'000	Carrying amount KShs'000	Fair value of collateral held KShs'000
Carrying amount	9,353,192	(1,442,146)	7,911,046	24,803,562

Loss allowance

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

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

Write-off policy

The Group writes off a loan balance (and any related allowances for impairment losses) when Group Credit determines that the loans are uncollectible. This is reached after considering information such as the occurrence of significant changes in the borrower/issuer's financial position such that the borrower / issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. The Group still seeks to recover amounts it is legally owed in full, but which have been partially written off due to no reasonable expectation of full recovery.

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Collateral and other credit enhancements - continued

Modification of financial assets

The Group sometimes modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximising recovery. Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Group has made concessions that it would not otherwise consider.

Such restructuring activities include extended payment term arrangements. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Restructuring is most commonly applied to term loans. The risk of default of such assets after modification is assessed at the reporting date and compared with the risk under the original terms at initial recognition, when the modification is not substantial and so does not result in derecognition of the original asset. The Group monitors the subsequent performance of modified assets. The Group may determine that the credit risk has significantly improved after restructuring, so that the assets are moved from Stage 3 or Stage 2 (Lifetime ECL) to Stage 1 (12-month ECL). This is only the case for assets which have performed in accordance with the new terms for six consecutive months or more. This is only the case for assets which have performed in accordance with the new terms for six consecutive months or more.

Concentration by Sector

The Group monitors concentrations of credit risk by sector. An analysis of concentrations of credit risk at the reporting date is shown below:

Concentration by Sector	2020	2019
	KShs'000	KShs'000
Agriculture	957,372	818,351
Manufacturing	1,792,249	1,555,477
Building and construction	205,406	235,489
Trade	2,826,169	2,739,231
Tourism, restaurants, and hotels	352,646	303,395
Transport and communication	334,443	299,024
Real estate	3,354,865	2,949,792
Financial services	15,939	28,305
Personal households	349,985	480,224
	<u>10,189,074</u>	<u>9,409,288</u>



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(a) Credit risk (continued)

Exposure to credit risk

	2020		2019	
	Group KShs'000	Bank KShs'000	Group KShs'000	Bank KShs'000
Balances with Central Bank of Kenya	682,875	682,875	361,419	361,419
Deposits and balances due from banking institutions	2,582,928	2,582,928	923,395	923,395
Loans and advances	8,609,289	8,609,289	7,911,046	7,911,046
Financial assets at fair value through profit and loss	103,177	103,177	101,767	101,767
Financial assets at amortised cost	3,952,870	3,931,826	4,553,553	4,532,494
Other assets	174,274	174,274	226,096	226,096
Financial assets at fair value through profit or loss	669,245	669,245	825,413	825,413
	<u>16,774,658</u>	<u>16,753,614</u>	<u>14,902,689</u>	<u>14,881,630</u>

(b) Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations from its financial liabilities.

Management of liquidity risk

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

Treasury receives information from other departments of the bank regarding cash requirements and integrates this information in form of projected cash flows. Treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the bank as a whole.

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 ALCO. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO.

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(b) Liquidity risk (continued)

Exposure to liquidity risk

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

	2020	2019
At 31 December	22.6%	8.3%
Average for the period	18.3%	6.4%
Maximum for the period	25.2%	13.2%
Minimum for the period	7.6%	1.2%



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(b) Liquidity risk (continued)

The table below analyses the Company's financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date. The amounts disclosed in the table below are the contractual cash flows :

Group	0 to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
At 31 December 2020						
Liabilities						
Due to banking institutions	228,879	1,671,604	177,052	-	-	2,077,535
Customer deposits	2,254,567	1,911,154	1,669,934	337,310	2,000	6,174,965
Borrowings	3,833,194	77,201	76,124	664,851	21,163	4,672,533
Lease liabilities	6,732	-	20,197	141,207	94,185	262,321
Other liabilities	53,442	6,954	44,884	44,884	142,469	292,633
Total liabilities	6,376,814	3,666,913	1,988,191	1,188,252	259,817	13,479,987
At 31 December 2019						
Liabilities						
Due to banking institutions	392,743	546,462	-	-	-	939,205
Customer deposits	2,503,259	1,731,859	649,255	4,234	176,078	5,064,685
Borrowings	4,429,079	74,138	70,557	282,231	21,163	4,877,168
Lease liabilities	28,059	6,325	19,383	82,982	179,342	316,091
Other liabilities	37,174	37,655	74,348	111,522	58,224	318,923
Total liabilities	7,390,314	2,396,439	813,543	480,969	434,807	11,516,072

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(b) Liquidity risk (continued)

Group

At 31 December 2020	0 to 1 month KShs'000	1 to 3 months KShs'000	3 to 12 months KShs'000	1 to 5 years KShs'000	Over 5 years KShs'000	Total KShs'000
Assets						
Cash and balances with Central Bank of Kenya	434,665	-	-	-	248,210	682,875
Financial assets at fair value through P&L	-	-	-	-	103,177	103,177
Financial assets at amortised cost	-	-	154,612	1,353,999	2,444,259	3,952,870
Due from other banks	657,478	1,571,255	174,135	180,060	-	2,582,928
Loans and advances to customers	906,798	314,084	1,004,930	2,316,633	4,066,844	8,609,289
Financial assets at fair value through OCI	-	-	-	-	669,245	669,245
Other assets	43,658	21,829	43,658	43,658	21,471	174,274
Total assets	2,042,599	1,907,168	1,377,335	3,894,350	7,553,206	16,774,658
At 31 December 2019						
Assets						
Cash and balances with Central Bank of Kenya	361,419	-	-	-	-	361,419
Financial assets at fair value through P&L	-	-	-	-	101,767	101,767
Financial assets at amortised cost	-	-	605,499	2,147,700	1,800,354	4,553,553
Due from other banks	342,348	554,834	-	26,213	-	923,395
Loans and advances to customers	1,326,791	641,144	1,575,838	1,465,122	2,902,151	7,911,046
Financial assets at fair value through OCI	-	-	-	-	825,413	825,413
Other assets	60,817	29,247	76,714	29,247	30,071	226,096
Total assets	2,091,375	1,225,225	2,258,051	3,668,282	5,659,756	14,902,689



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk

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

Management of market risks

Overall authority for market risk is vested in ALCO. The Group separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios mainly are held by the Treasury Department, and include positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

The Group is primarily exposed to interest rate risk and foreign exchange risk.

(i) Interest rate risk

This 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. Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the Group's interest rate gap position reflecting assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates is shown on the next page.

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various standard and non-standard interest rate scenarios. Standard scenarios that are considered on a regular basis include a 100, 50, and 25 basis point (bp) parallel fall or rise in all yield curves. An analysis of the Group's sensitivity to an increase or decrease in market interest rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position) is as follows:

	2020 KShs '000	2019 KShs '000
100 Basis points upward parallel shift	(7,108)	(7,650)
50 Basis points upward parallel shift	(2,449)	(2,643)
25 Basis points upward parallel shift	(1,234)	(1,334)
100 Basis points downward parallel shift	1,255	1,358
50 Basis points downward parallel shift	2,530	2,741
25 Basis points downward parallel shift	5,146	5,585



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk (continued)

(i) Interest rate risk - continued

The table below summarises the exposure to interest rate risks. Included in the table below are the Bank's assets and liabilities for 2020 at carrying amounts categorised by the earlier of contractual repricing or maturity dates.

Group

	Effective interest rate	0 to 3 months KShs'000	3 to 12 months KShs'000	1 to 5 years KShs'000	Over 5 years KShs'000	Non-interest bearing KShs'000	Total KShs'000
Assets							
Cash and balances with Central Bank of Kenya	-	-	-	-	-	682,875	682,875
Financial assets at fair value through P&L	11.25	-	-	-	103,177	-	103,177
Financial assets at amortised cost	11.76	-	154,612	1,353,999	2,444,259	-	3,952,870
Due from banking institutions	3.62	370,514	2,021,134	191,280	-	-	2,582,928
Loans and advances to customers	11.75	1,220,882	1,004,930	2,316,633	4,066,844	-	8,609,289
Other assets	-	-	-	-	-	174,274	174,274
Total assets		1,591,396	3,180,676	3,861,912	6,614,280	857,149	16,105,413
Liabilities							
Due to banking institutions	1.24	10,079	45,055	2,022,401	-	-	2,077,535
Customers' deposits	8.80	4,165,721	1,669,934	337,310	2,000	-	6,174,965
Borrowings	6.42	3,910,395	76,124	664,851	21,163	-	4,672,533
Other liabilities	-	-	-	-	-	292,633	292,633
Total liabilities		8,086,195	1,791,113	3,024,562	23,163	292,633	13,217,666



Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk (continued)

(i) Interest rate risk - continued

The table below summarises the exposure to interest rate risks. Included in the table below are the Bank's assets and liabilities for 2019 at carrying amounts categorised by the earlier of contractual repricing or maturity dates.

Group

	Effective interest rate	0 to 3 months KShs'000	3 to 12 months KShs'000	1 to 5 years KShs'000	Over 5 years KShs'000	Non- interest bearing KShs'000	Total KShs'000
Assets							
Cash and balances with Central Bank of Kenya	-	-	-	-	-	361,419	361,419
Financial assets at fair value through P&L	11.25	-	-	-	101,767	-	101,767
Financial assets at amortised cost	11.45	-	605,499	2,147,700	1,800,354	-	4,553,553
Due from banking institutions	4.14	897,182	-	26,213	-	-	923,395
Loans and advances to customers	11.07	1,967,935	1,575,838	1,465,122	2,902,151	-	7,911,046
Other assets	-	-	-	-	-	226,096	226,096
Total assets		2,865,117	2,181,337	3,639,035	4,804,272	587,515	14,077,276
Liabilities							
Due to banking institutions	1.24	939,205	-	-	-	-	939,205
Customers' deposits	8.36	4,235,118	649,255	4,234	176,078	-	5,064,685
Borrowings	7.97	4,503,217	70,557	282,231	21,163	-	4,877,168
Other liabilities		-	-	-	-	318,923	318,923
Total liabilities		9,677,540	719,812	286,465	197,241	318,923	11,199,981

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk (continued)

(i) Interest rate risk - continued

The table below summarises the exposure to interest rate risks. Included in the table below are the Bank's assets and liabilities for 2020 at carrying amounts categorised by the earlier of contractual repricing or maturity dates.

Bank

	Effective interest rate	0 to 3 months KShs'000	3 to 12 months KShs'000	1 to 5 years KShs'000	Over 5 years KShs'000	Non- interest bearing KShs'000	Total KShs'000
Assets							
Cash and balances with Central Bank of Kenya	-	-	-	-	-	682,875	682,875
Financial assets at fair value through P&L	11.25	-	-	-	103,177	-	103,177
Financial assets at amortised cost	11.76	-	154,612	1,353,999	2,423,215	-	3,931,826
Due from banking institutions	3.62	370,514	2,021,134	191,280	-	-	2,582,928
Loans and advances to customers	11.75	1,220,882	1,004,930	2,316,633	4,066,844	-	8,609,289
Other assets	-	-	-	-	-	174,274	174,274
Total assets		1,591,396	3,180,676	3,861,912	6,593,236	857,149	16,084,369
Liabilities							
Due to banking institutions	1.24	10,079	45,055	2,022,401	-	-	2,077,535
Customers' deposits	8.80	4,192,703	1,669,934	337,310	2,000	-	6,201,947
Borrowings	6.42	3,910,395	76,124	664,851	21,163	-	4,672,533
Other liabilities		-	-	-	-	291,521	291,521
Total liabilities		8,113,177	1,791,113	3,024,562	23,163	291,521	13,243,536

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk (continued)

(i) Interest rate risk - continued

The table below summarises the exposure to interest rate risks. Included in the table below are the Bank's assets and liabilities for 2019 at carrying amounts categorised by the earlier of contractual repricing or maturity dates.

Bank

	Effective interest rate	0 to 3 months KShs'000	3 to 12 months KShs'000	1 to 5 years KShs'000	Over 5 years KShs'000	Non-interest bearing KShs'000	Total KShs'000
Assets							
Cash and balances with Central Bank of Kenya		-	-	-	-	361,419	361,419
Financial assets at fair value through P&L	11.25	-	-	-	101,767	-	101,767
Financial assets at amortised cost	11.45	-	605,499	2,147,700	1,779,295	-	4,532,494
Due from banking institutions	4.14	897,182	-	26,213	-	-	923,395
Loans and advances to customers	11.07	1,967,935	1,575,838	1,465,122	2,902,151	-	7,911,046
Other assets		-	-	-	-	226,095	226,095
Total assets		2,865,117	2,181,337	3,639,035	4,783,213	587,514	14,056,216
Liabilities							
Due to banking institutions	1.24	939,205	-	-	-	-	939,205
Customers' deposits	8.36	4,260,512	649,255	4,234	176,078	-	5,090,079
Borrowings	7.97	4,503,217	70,557	282,231	21,163	-	4,877,168
Other liabilities		-	-	-	-	318,032	318,032
Total liabilities		9,702,934	719,812	286,465	197,241	318,032	11,224,484

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk (continued)

(ii) Currency risk

The Group is exposed to currency risk through transactions in foreign currencies. The Group's transactional exposures give rise to foreign currency gains and losses that are recognised in profit or loss. In respect of monetary assets and liabilities in foreign currencies, the Group ensures that its net exposure is kept to an acceptable level by buying and selling foreign currencies at spot rates when considered appropriate.

The table below analyses the currencies to which the Group and the Bank are exposed at 31 December 2020:

At 31 December 2020	USD KShs'000	GBP KShs'000	Euro KShs'000	Other KShs'000	Total KShs'000
Assets					
Cash and balances with Central Bank of Kenya	116,321	3,157	100,057	697	220,232
Deposits and balances due from banking institutions	653,666	-	157,746	-	811,412
Loans and advances to customers	355,163	-	1,177,918	-	1,533,081
Other assets	-	-	-	-	-
Total foreign currency assets	1,125,150	3,157,	1,435,721	697	2,564,725
Liabilities					
Borrowings	303,862	48	-	-	303,910
Deposits and balances due to banking institutions	600,441	-	1,405,903	-	2,006,344
Deposit and balance due to customers	43,174	2,667	5,795	-	51,636
Other liabilities	-	-	-	-	-
Total foreign currency liabilities	947,477	2,715	1,411,698	-	2,361,890
Foreign currency exposure at 31 December 2020	177,673	442	24,023	697	202,835

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(c) Market risk (continued)

(ii) Currency risk - continued

The Group is exposed to currency risk through transactions in foreign currencies. The Group's transactional exposures give rise to foreign currency gains and losses that are recognised in profit or loss. In respect of monetary assets and liabilities in foreign currencies, the Group ensures that its net exposure is kept to an acceptable level by buying and selling foreign currencies at spot rates when considered appropriate.

The table below analyses the currencies to which the Group and the Bank are exposed at 31 December 2019:

At 31 December 2019	USD KShs'000	GBP KShs'000	Euro KShs'000	Other KShs'000	Total KShs'000
Assets					
Cash and balances with Central Bank of Kenya	59,999	1,266	5,570	268	67,103
Deposits and balances due from banking institutions	48,970	1,198	5,482	81	55,731
Loans and advances to customers	722,160	-	592,237	-	1,314,397
Other assets	-	-	-	-	-
Total foreign currency assets	831,129	2,464	603,289	349	1,437,231
Liabilities					
Borrowings	426,926	-	-	-	426,926
Deposits and balances due to banking institutions	202,800	-	614,992	-	817,792
Deposit and balance due to customers	78,951	1,058	4,056	-	84,065
Other liabilities	-	-	-	-	-
Total foreign currency liabilities	708,677	1,058	619,048	-	1,328,783
Foreign currency exposure at 31 December 2019	122,452	1,406	(15,759)	349	108,448

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(d) Capital management

The Central Bank of Kenya sets and monitors capital requirements for the Group as a whole.

In implementing current capital requirements the Central Bank of Kenya requires the bank to maintain a prescribed ratio of total capital to total risk-weighted assets.

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

- Tier 1 capital, which includes ordinary share capital, share premium, perpetual bonds (which are classified as innovative Tier 1 securities), retained earnings, translation reserve and minority interests after deductions for goodwill and intangible assets, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.
- Tier 2 capital, which includes qualifying subordinated liabilities, collective impairment allowances and the element of the fair value reserve relating to unrealised gains on equity instruments classified as available-for-sale.

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Group recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Group has complied with all externally imposed capital requirements throughout the period. There have been no material changes in the Group's management of capital during the period.

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

	2020	2019
	KShs'000	KShs'000
Core capital (Tier 1)		
Paid up share capital	1,042,500	1,042,500
Retained earnings	1,352,202	1,606,267
Other reserves	281	281
Core capital	2,394,983	2,649,048
Minimum statutory capital	1,000,000	1,000,000
Excess capital	1,394,983	1,649,048
Supplementary capital (Tier 2)	300,127	303,055
Total capital	2,695,110	2,952,103
Total risk weighted assets	8,128,605	9,381,519

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(d) Capital management (continued)

Capital adequacy ratios

	2020	2019
Percentage of Core Capital to Risk Weighted Asset ratio	19.8%	28.2%
Minimum requirement	10.5%	10.5%
Percentage of Total Capital to Risk Weighted Asset ratio	22.2%	31.5%
Minimum requirement	14.5%	14.5%
Percentage of Core Capital to Deposits ratio	38.3%	50.9%
Minimum requirement	8.0%	8.0%

(e) Fair value measurement

Fair value hierarchy

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

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

As at 31 December 2020	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Total KShs'000
Assets				
Fair value through profit or loss	-	103,177	-	103,177
Fair value through other comprehensive income	-	-	669,245	669,245
Loans and advances	-	-	8,609,289	8,609,289
Total assets	-	103,177	9,278,534	9,411,711
As at 31 December 2019	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Total KShs'000
Assets				
Fair value through profit or loss	-	101,767	-	101,767
Fair value through other comprehensive income	-	-	825,413	825,413
	-	-	7,911,046	7,911,046
Total assets	-	101,767	8,736,459	8,838,226

Notes to the financial statements (Continued)

4. Financial risk management (Continued)

(e) Fair value measurement (continued)

Financial instruments in level 2

The fair value of these financial assets is determined by using valuation techniques which maximize the use of observable market data where it is available and rely as little as possible on entity specific estimates. Specifically, the directors have used the discounted cash flow technique using quoted yields for the same or similar products.

5. Interest income

Group

	2020	2019
	KShs'000	KShs'000
Loans and advances to customers	324,649	382,075
Overdrafts	333,017	393,496
Financial assets at fair value through profit and loss	12,051	16,980
Financial assets at amortised cost	460,118	509,487
Deposits and balances due from banking institutions	84,090	34,046
	<u>1,213,925</u>	<u>1,336,084</u>

Bank

Loans and advances to customers	324,649	382,075
Overdrafts	333,017	393,496
Financial assets at fair value through profit and loss	12,051	16,980
Financial assets at amortised cost	457,883	507,252
Deposits and balances due from banking institutions	84,090	34,046
	<u>1,211,690</u>	<u>1,333,849</u>

Included within interest income on investment securities for the year ended 31 December 2020 is KShs 457,883,000 (2019 - KShs 507,252,000) relating to debt securities held at amortised cost

6. Interest expense

Group

	2020	2019
	KShs'000	KShs'000
Customer deposits	515,743	475,247
Deposits and balances due to banking institutions	74,711	18,195
Borrowings	258,367	435,358
	<u>848,821</u>	<u>928,800</u>

Notes to the financial statements (Continued)

6. Interest expense (Continued)

Bank	2020	2019
	KShs'000	KShs'000
Customer deposits	516,303	475,810
Deposits and balances due to banking institutions	74,711	18,195
Borrowings	258,367	435,358
	849,381	929,363

7. Net fees and commissions income

Group and Bank

Commissions on loans and advances	7,984	3,995
Other fees	14,247	11,886
	22,231	15,881

Other fees relate to ledger fee

8. Other operating income

Group

(i) Profit from sale of Finance House **-** **1,062,588**

(ii) Other operating income

Gains arising from dealing in foreign currencies	81,150	28,814
Other income	610	36,421
	81,760	65,235

Bank

(i) Profit from sale of Finance House **-** **1,062,588**

(ii) Other operating income

Gains arising from dealing in foreign currencies	81,150	28,814
Other income	610	36,171
	81,760	64,985

9. Operating expenses

Group

Salaries and employee benefits (Note 10)	207,477	218,095
Occupancy expenses	12,864	48,962
Deposit Protection Fund	8,633	9,544
Depreciation	70,789	23,268
Directors' emoluments	17,608	15,053
Professional and legal services	15,650	23,000
Telecommunication	3,982	3,352
Other expenses	80,414	62,394
	417,417	403,668



Notes to the financial statements (Continued)

	2020	2019
	KShs'000	KShs'000
9. Operating expenses (Continued)		
Bank		
Salaries and employee benefits (Note 10)	207,477	218,095
Occupancy expenses	12,864	48,962
Deposit Protection Fund	8,633	9,544
Depreciation	70,789	23,268
Directors' emoluments	17,508	14,953
Professional and legal services	15,650	23,000
Telecommunication	3,982	3,352
Other expenses	79,738	61,804
	<u>416,641</u>	<u>402,978</u>
10. Salaries and employee benefits		
Group and Bank		
Salaries	156,770	166,709
Contributions to defined contribution plans	18,590	18,797
National Social Security Fund	921	758
Other staff costs	31,196	31,831
	<u>207,477</u>	<u>218,095</u>
11. Profit before taxation		
Profit before taxation is arrived at after charging:		
Group		
Depreciation expense (Note 25)	70,789	23,269
Director's emoluments:		
– Fees as non-executive	1,900	1,600
– Other*	15,708	13,453
Auditors' remuneration	2,650	2,650
	<u>2,650</u>	<u>2,650</u>
Bank		
Depreciation expense (Note 25)	70,789	23,269
Director's emoluments:		
– Fees as non-executive	1,800	1,500
– Other*	15,708	13,453
Auditors' remuneration	2,400	2,400
	<u>2,400</u>	<u>2,400</u>

* Directors emoluments 'other' include sitting allowances, chairman's honorarium and director's travel expenses.

Notes to the financial statements (Continued)

12. Income tax expense

Group	2020		2019	
	Group KShs'000	Company KShs'000	Group KShs'000	Company KShs'000
Current income tax	440	-	44,178	43,438
Deferred income tax (Note 24)	(1,729)	(1,699)	14,241	14,271
	<u>1,289</u>	<u>(1,699)</u>	<u>58,419</u>	<u>57,709</u>

The tax on the Group's profit differs from the theoretical amount using the basic tax rate as follows:

Group	2020	2019
	KShs'000	KShs'000
Accounting profit before tax	20,541	1,139,192
Computed tax using the applicable corporation tax rate of 25% (2019 – 30%)	5,135	341,758
Profit on sale of building at reduced rate of 5%	-	(275,340)
Deferred tax at 30%	339	-
Tax impact of expenses not deductible for tax purposes	(6,763)	(7,999)
Income tax expense	<u>(1,289)</u>	<u>58,419</u>
Bank		
Accounting profit before tax	18,880	1,136,824
Computed tax using the applicable corporation tax rate of 25% (2019 – 30%)	4,720	341,048
Profit on sale of building at reduced rate of 5%	-	(275,340)
Deferred tax at 30%	344	-
Tax impact of expenses not deductible for tax purposes	(6,763)	(7,999)
Income tax expense	<u>(1,699)</u>	<u>57,709</u>

13. Equity investment designated as FVOCI

Group and Bank

Revaluation loss on equity investment	(156,168)	-
Related deferred tax	7,808	-
	<u>(148,360)</u>	<u>-</u>

14. Dividend per share

The Bank did not pay an interim dividend in the year (2019 – Nil). The company does not propose payment of a final dividend (2019 – Nil).

Notes to the financial statements (Continued)

15. Earnings per share

The calculation of basic earnings per share is based on:

Group	2020	2019
Net profit for the year attributable to shareholders (KShs '000)	21,830	1,080,773
Number of ordinary shares ('000)	52,125	52,125
Earnings per share (KShs)	<u>0.42</u>	<u>20.73</u>
Bank		
Net profit for the year attributable to shareholders (KShs '000)	20,579	1,079,115
Number of ordinary shares ('000)	52,125	52,125
Earnings per share (KShs)	<u>0.39</u>	<u>20.70</u>

There were no potentially dilutive shares outstanding at 31 December 2020 and 2019.

16. Cash and balances with Central Bank of Kenya

Group and Bank	2020 KShs'000	2019 KShs'000
Cash on hand	88,319	34,130
Balances with Central Bank of Kenya:		
— Local currency cash reserve ratio	248,210	274,289
— Other	346,346	53,000
	<u>682,875</u>	<u>361,419</u>

The cash reserve ratio is non-interest earning and is based on the value of deposits as adjusted for Central Bank of Kenya requirements. At 31 December 2020, the cash reserve requirement was 4.25% (2019 – 5.25%) of all customer deposits. These funds are available to finance the bank's day-to-day operations in a limited way provided that on any given day the balance does fall below the 3% minimum daily requirements and provided that the overall average in the month is at least 5.25%.

17. Financial assets (Investment in government securities)

Group	2020 KShs'000	2019 KShs'000
Financial assets at amortised cost		
<i>Treasury bonds:</i>		
Maturing within one year	154,612	605,499
Maturing after one year	3,798,258	3,948,054
Total held to maturity	<u>3,952,870</u>	<u>4,553,553</u>
Financial assets at fair value through profit and Loss		
<i>Treasury bonds:</i>		
Maturing after one year	103,177	101,767
	<u>4,056,047</u>	<u>4,655,320</u>

Notes to the financial statements (Continued)

17. Financial assets (Continued)	2020	2019
Bank	KShs'000	KShs'000
Financial Assets at amortised cost		
<i>Treasury bonds:</i>		
Maturing within one year	154,612	605,499
Maturing after one year	3,777,214	3,926,995
Total held to maturity	<u>3,931,826</u>	<u>4,532,494</u>
Financial assets at fair value through profit and Loss		
<i>Treasury bonds:</i>		
Maturing after one year	103,177	101,767
	<u>4,035,003</u>	<u>4,634,261</u>

The weighted average effective interest rate on government securities at 31 December 2020 was 11.76% (2019 – 11.45%).

18. Deposits and balances due from banking institutions	2020	2019
Group and Bank	KShs'000	KShs'000
Due within 90 days	2,228,733	897,182
Due between 3 months and 1 year	174,135	-
Due between 1 year and 5 year	180,060	26,213
	<u>2,582,928</u>	<u>923,395</u>

The weighted average effective interest rate on placements with other banks at 31 December 2020 was 3.62% (2019 – 5.81%).

19. Loans and advances to customers	2019	
	Group	Bank
	KShs'000	KShs'000
Overdrafts	4,236,662	4,236,662
Loans	4,886,150	4,830,054
Staff loans	286,476	286,476
	9,409,288	9,353,192
Less: ECL allowance	<u>(1,498,242)</u>	<u>(1,442,146)</u>
	<u>7,911,046</u>	<u>7,911,046</u>
Maturing within 1 year	3,543,773	3,543,773
Between 1 and 3 years	499,098	499,098
Over 3 years	3,868,175	3,868,175
	<u>7,911,046</u>	<u>7,911,046</u>

Notes to the financial statements (Continued)

19. Loans and advances (Continued)

	2020	
	Group KShs '000	Bank KShs '000
Overdrafts	4,622,612	4,622,612
Loans	5,273,699	5,217,700
Staff loans	292,763	292,763
	10,189,074	10,133,075
Less: ECL allowance	(1,579,785)	(1,523,786)
	8,609,289	8,609,289
Maturing within 1 year	2,241,750	2,241,750
Between 1 and 3 years	799,359	799,359
Over 3 years	5,568,180	5,568,180
	8,609,289	8,609,289

The weighted average effective interest rate on loans and advances to customers at 31 December 2020 was 11.75% (2019 – 11.07%).

Impairment losses on loans and advances charged to profit or loss

Group	2020	2019
	KShs'000	KShs'000
Provisions during the year	95,969	160,685
Recovered during the year	(65,184)	(152,615)
Direct write offs	352	58
	31,137	8,128
Bank		
Provisions during the year	95,747	160,685
Recovered during the year	(65,134)	(152,605)
Direct write offs	166	58
	30,779	8,138

20. Financial assets at fair value through other comprehensive income

Group and Bank

Unquoted shares measured at fair value through other comprehensive income - refer to note 13.	2020	2019
	KShs'000	KShs'000
Kenya Hotel Properties Plc		
2,258,017 ordinary shares of KShs 20 each		
At 1 January	825,413	825,413
Revaluation loss on equity investment	(156,168)	-
	669,245	825,413

Notes to the financial statements (Continued)

20. Financial assets at fair value (continued) through other comprehensive income (Continued)

	2020	2019
	KShs'000	KShs'000
Chemilil Sugar Company Limited 150,000 ordinary shares of KShs 20 each	3,000	3,000
Pan African Paper Mills Limited 104,000 ordinary shares at KShs 20	2,080	2,080
Kenya United Steel Company Limited 180,000 ordinary shares of KShs 5 each	900	900
East African Sugar Industries Limited 100,000 ordinary shares of KShs 20 each	2,000	2,000
	<u>7,980</u>	<u>7,980</u>
Impairment allowance	(7,980)	(7,980)
Net carrying amount of unquoted shares (impaired)	<u>-</u>	<u>-</u>
Net carrying amount of equity investments	<u>669,245</u>	<u>825,413</u>

21. Investment in subsidiary

Bank	2020	2019
	KShs'000	KShs'000
Shares at cost:		
Small Enterprises Finance Company Limited (SEFCO)	<u>32,048</u>	<u>32,048</u>

SEFCO is a wholly owned subsidiary of the bank. The subsidiary company is incorporated in Kenya.

22. Tax recoverable/(payable)

	2020		2019	
	Group	Bank	Group	Bank
	KShs'000	KShs'000	KShs'000	KShs'000
As at 1 January	30,057	27,119	347	(3,022)
Tax expense (Note 12)	(440)	-	(44,178)	(43,438)
Tax paid	310	-	73,888	73,579
	<u>29,927</u>	<u>27,119</u>	<u>30,057</u>	<u>27,119</u>

23. Other assets

	2020		2019	
	Group	Bank	Group	Bank
	KShs'000	KShs'000	KShs'000	KShs'000
Rent receivable	4,418	4,418	4,861	4,861
Uncleared effects	7,014	7,014	2,323	2,323
Prepayments	20,513	20,513	16,706	16,706
Due from ICDC	128,587	128,587	189,079	189,079
Other receivables	13,742	13,742	13,127	13,126
	<u>174,274</u>	<u>174,274</u>	<u>226,096</u>	<u>226,095</u>

Notes to the financial statements (Continued)

24. Deferred income tax

Deferred income tax is calculated in full on all temporary differences under the liability method using a principal tax rate of 30% (2019 – 30%). The movement on the deferred tax account is as follows:

	Group KShs'000	Bank KShs'000
2019		
At start of the year	116,082	115,961
Charged to profit or loss	(14,241)	(14,271)
Charged to other comprehensive income	-	-
	<u>101,841</u>	<u>101,690</u>
2020		
At start of the year	101,841	101,690
Credit to profit or loss	1,729	1,699
Charged to other comprehensive income	7,808	7,808
	<u>111,378</u>	<u>111,197</u>

The deferred income tax assets and liabilities, deferred tax credit/(charge) in the statement of profit or loss are attributable to the following items:

Group	At 1 January KShs'000	(Charge)/ credit to profit or loss KShs'000	At 31 December KShs'000
Deferred income tax liabilities			
Fair value gain on equity investments	(39,113)	-	(39,113)
Deferred income tax assets			
Property and equipment	17,947	(9,493)	8,454
Right of use assets	-	3,167	3,167
Portfolio impairment provisions on loans and advances	133,212	(13,285)	119,927
Tax loss	-	5,362	5,362
Other provisions	4,036	8	4,044
	<u>155,195</u>	<u>(14,241)</u>	<u>140,954</u>
	<u>116,082</u>	<u>(14,241)</u>	<u>101,841</u>

Notes to the financial statements (Continued)

24. Deferred income tax (Continued)

2020	At 1 January	(Charge)/ credit to profit or loss	At 31
	KShs'000	KShs'000	December
			KShs'000
Deferred income tax liabilities			
Fair value gain on equity investments	(39,113)	7,808	(31,305)
Deferred income tax assets			
Property and equipment	8,454	4,690	13,144
Right of use assets	3,167	2,392	5,559
Portfolio impairment provisions on loans and advances	119,927	(3,342)	116,585
Tax loss	5,362	(2,859)	2,503
Other provisions	4,044	848	4,892
	140,954	1,729	142,683
	101,841	9,537	111,378
Bank			
2019			
Deferred income tax liabilities			
Fair value gain on equity investments	(39,113)	-	(39,113)
Deferred income tax assets			
Property and equipment	17,947	(9,493)	8,454
Right of use assets	-	3,167	3,167
Portfolio impairment provisions on loans and advances	133,212	(13,285)	119,927
Tax loss	-	5,362	5,362
Other provisions	3,915	(22)	3,893
	155,074	(14,271)	140,803
	115,961	(14,271)	101,690
2020			
Deferred income tax liabilities			
Fair value gain on equity investments	(39,113)	7,808	(31,305)
Deferred income tax assets			
Property and equipment	8,454	4,690	13,144
Right of use assets	3,167	2,392	5,559
Portfolio impairment provisions on loans and advances	119,927	(3,342)	116,585
Tax loss	5,362	(2,859)	2,503
Other provisions	3,893	818	4,711
	140,803	1,699	142,502
	101,690	9,507	111,197

Notes to the financial statements (Continued)

24. Deferred income tax (Continued)

Tax losses expire after nine (9) years following the year in which they arose under the current tax legislation. Notwithstanding, the Minister may, on recommendation of the Commissioner, extend the period of deduction beyond ten years where a person applies through the Commissioner for such extension, giving evidence of inability to extinguish the deficit within the period.

Bank	Taxable (loss)/profit KShs'000	Year of expiry
Year of origin 2019	<u>17,874</u>	2028
	<u><u>17,874</u></u>	

Notes to the financial statements (Continued)

25. Property and equipment

Group and Bank 2019	Right of Use Assets KShs'000	Leasehold improvements KShs'000	Furniture and equipment KShs'000	Computers KShs'000	Motor vehicles KShs'000	Capital work in progress KShs'000	Total KShs'000
Cost							
At 1 January 2019	17,347	60,614	34,547	47,611	38,034	107,655	305,808
Additions	148,012	-	906	36,349	-	14,043	199,310
Transfer from Capital Work in Progress	-	-	-	117,959	-	(117,959)	-
At 31 December 2019	165,359	60,614	35,453	201,919	38,034	3739	505,118
Depreciation							
At 1 January 2019	-	(56,733)	(30,707)	(41,509)	(37,317)	-	(166,266)
Charge for the year	(14,503)	(2,394)	(1,087)	(4,568)	(717)	-	(23,269)
At 31 December 2019	(14,503)	(59,127)	(31,794)	(46,077)	(38,034)	-	(189,535)
Net book amount at 31 December	150,856	1,487	3,659	155,842	-	3,739	315,583

Notes to the financial statements (Continued)

25. Property and equipment (Continued)

Group and Bank 2020	Right of Use Assets KShs'000	Leasehold improvements KShs'000	Furniture and equipment KShs'000	Computers KShs'000	Motor vehicles KShs'000	Capital work in progress KShs'000	Total KShs'000
Cost							
At 1 January 2020	165,359	60,614	35,453	201,919	38,034	3,739	505,118
Additions	-	588	7,296	9,449	-	36,107	53,440
At 31 December 2020	165,359	61,202	42,749	211,368	38,034	39,846	558,558
Depreciation							
At 1 January 2020	(14,503)	(59,127)	(31,794)	(46,077)	(38,034)	-	(189,535)
Charge for the year	(14,503)	(427)	(1,212)	(54,647)	-	-	(70,789)
At 31 December 2020	(29,006)	(59,554)	(33,006)	(100,724)	(38,034)	-	(260,324)
Net book amount at 31 December	136,353	1,648	9,743	110,644	-	39,846	298,234

As at 31 December 2020, property and equipment includes right-of-use assets of KShs 136,353,000 (2019 - KShs 150,856 000) related to leased branches and office premises (see Note 32).

As at 31 December, property and equipment with a value of KShs 160,786,180 (2019 – KShs 109,804,987) were fully depreciated. Their notional depreciation is KShs 35,094,373 (2019 – KShs 25,533,687)

Notes to the financial statements (Continued)

26. Deposits and balances due to banking institutions

Group and Bank	2020 KShs'000	2019 KShs'000
Payable within 90 days	1,900,483	939,205
Payable between 3 months and one year	<u>177,052</u>	<u>-</u>
	<u>2,077,535</u>	<u>939,205</u>

The weighted average effective interest rate on deposits from other banks at 31 December 2020 was 1.24% (2019 – 1.24%).

27. Customer deposits

	2020		2019	
	Group KShs'000	Bank KShs'000	Group KShs'000	Bank KShs'000
From government and parastatals	473,013	473,013	1,056,410	1,056,410
From private sector and individuals	<u>5,701,952</u>	<u>5,728,934</u>	<u>4,008,275</u>	<u>4,033,669</u>
	<u>6,174,965</u>	<u>6,201,947</u>	<u>5,064,685</u>	<u>5,090,079</u>

Included in the Company customer's deposits is KShs 26,982,000 (2019 – KShs 25,394,000) due to the subsidiary company. Interest paid on these deposits during the year amounted to KShs 560,000(2019 - KShs 563,000).

The weighted average effective interest rate on customer deposits at 31 December 2020 was 8.80% (2019 – 8.36%).

28. Borrowings

Group and Bank	2020 KShs'000	2019 KShs'000
European Investment Bank	21,163	21,163
Central Bank of Kenya	3,833,194	4,429,079
Industrial and Commercial Development Corporation (ICDC)	512,603	-
China Development Bank	<u>305,573</u>	<u>426,926</u>
	<u>4,672,533</u>	<u>4,877,168</u>

Group and Bank

Maturities

Less than one year	3,833,194	4,573,774
Between one and five years	818,176	282,231
Over 5 years	<u>21,163</u>	<u>21,163</u>
	<u>4,672,533</u>	<u>4,877,168</u>

Notes to the financial statements (Continued)

28. Borrowings (Continued)

The weighted average effective interest rate on loan capital at 31 December 2020 was 6.42% (2019: 7.97%).

Loan terms

- The loan from China Development Bank was disbursed in 2008 and 2009 and is to be repaid over a period of 15 years. The loan matures in 2022. The loan is payable half yearly and interest is charged at 6 months LIBOR plus margin of 0.8%.
- Borrowings from the Central Bank of Kenya comprise of short term borrowings of up to 1 month at an average interest rate of 9% p.a.

29. Other liabilities

	2020		2019	
	Group KShs'000	Bank KShs'000	Group KShs'000	Bank KShs'000
Bills payable	7,446	7,446	6,616	6,616
Rent deposit	18,618	18,618	18,618	18,618
Deutsche Investitions-und EntwicklungsgesellschaftmbH (DEG) retained funds	135,867	135,867	133,173	133,173
Payable to Government of Kenya	65,281	65,281	65,281	65,281
Provisions and accruals	49,025	49,025	79,122	77,902
Other liabilities	16,396	15,284	16,113	16,442
	292,633	291,521	318,923	318,032

30. Share capital

	2020 KShs'000	2019 KShs'000
Authorised, issued and fully paid 1 January and 31 December		
52,125,000 ordinary shares of KShs 20 each	1,042,500	1,042,500
	1,042,500	1,042,500

Total number of shares in issue 52,125,000 (2019 – 52,125,000).

All ordinary shares rank equally with regard to the company's residual assets. The holders of ordinary shares are entitled to receive dividend as declared from time to time and are entitled to one vote per share at the general meeting of the company.

Notes to the financial statements (Continued)

31. Cash and cash equivalents

	2020	2019
	KShs'000	KShs'000
Group and Bank		
Cash in hand (Note 16)	88,319	34,130
Cash at Central Bank of Kenya (Note 16)	346,346	53,000
Deposits and balances due from banks (Note 18)	2,228,733	897,182
Deposits and balances due to banks (Note 26)	<u>(1,900,483)</u>	<u>(939,205)</u>
	<u>762,915</u>	<u>45,107</u>

32. Leases

The Bank leases a number of premises for head office and the branches. The leases typically run for an initial period of between five and ten years with an option to renew the lease at the expiry of the lease.

Previously, these leases were classified as operating leases under IAS 17. The Bank used a number of practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17. In particular, the Company:

- relied on its assessment of whether leases are onerous under IAS 37 Provisions, Contingent Liabilities and Contingent Assets immediately before the date of initial application as an alternative to performing an impairment review;
- did not recognise right-of-use assets and liabilities for leases for which the lease term ends within 12 months of the date of initial application;
- did not recognise right-of-use assets and liabilities for leases of low-value assets (i.e. offices);
- excluded initial direct costs from measuring the right-of-use asset at the date of initial application; and
- used hindsight when determining the lease term

Information about leases for which the Bank is a lessee is presented below.

(a) Right-of-use assets

Right-of-use assets relate to leased head office and branch office premises that are presented within property and equipment under Note 25

	2020	2019
	Kshs '000	KShs'000
At 1 January	150,856	17,347
Additions	-	148,012
Depreciation charge for the year	<u>(14,503)</u>	<u>(14,503)</u>
At 31 December	<u>136,353</u>	<u>150,856</u>

As at 31 December, the future minimum lease payments under non-cancellable operating leases were payable as follows

Notes to the financial statements (Continued)

32. Leases (Continued)

(b) Lease liabilities

The movement in lease liabilities during the year is as follows:

	2020	2019
	KShs '000	KShs'000
At 1 January	183,146	17,347
Additions	-	148,012
Lease interest charge	19,390	20,553
Interest paid	(38,279)	(2,178)
Lease rental payment	(8,239)	(588)
At 31 December	<u>156,018</u>	<u>183,146</u>
(c) Amount recognised in profit or loss		
Finance cost on lease liabilities	<u>19,390</u>	<u>20,553</u>
At 31 December	<u>19,390</u>	<u>20,553</u>
(d) Amount recognised in the statement of cash flows		
Total cash outflow for leases	<u>46,518</u>	<u>2,765</u>

33. Contingencies

At any time the Group has outstanding commitments to extend credit. These commitments take the form of approved loans and overdraft facilities. At 31 December 2020, interest rates on loans and overdrafts ranged from 3.00% to 13.00% (2019 – 3.00% to 13.00%). The contractual amounts of commitments are set out below:

(a) Commitments to extend credit with respect to:

	2020	2019
	KShs'000	KShs'000
Undrawn loans	234,310	161,264
Undrawn overdraft facilities	12,000	7,150
Unutilised guarantees and letters of credit	<u>8,406</u>	<u>7,339</u>
	<u>254,716</u>	<u>175,753</u>

At 31 December 2020, interest rate on facilities subject to commitments ranged from 3.00% to 13.00% (2019 – 3.00% - 13.00%).

Notes to the financial statements (Continued)

33. Contingencies (Continued)

(b) Commitments with respect to outstanding off-balance items

	2020	2019
	KShs'000	KShs'000
Guarantees	801,086	668,642
Acceptances	11,851	105,870
Letters of credit	153,333	-
Undelivered spots	92	92
	<u>966,362</u>	<u>774,604</u>

(c) Nature of contingent liabilities

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

Guarantees 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 customers' default.

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

(d) Litigations against Small Enterprises Finance Company Limited (SEFCO)

Litigations against the subsidiary company, SEFCO, arising from normal cause of business have been lodged by some customers. The likely outcome of these cases cannot be objectively determined as at the date of signing of these financial statements. However, the Directors do not anticipate that any liability will arise from these suits.

34. Related party transactions

(a) Loans and advances to employees

	2020	2019
	KShs'000	KShs'000
At 1 January	288,228	281,740
Advances in the year	53,664	66,879
Repayments in the year	<u>(48,935)</u>	<u>(60,391)</u>
At 31 December	<u>292,957</u>	<u>288,228</u>

Interest earned on staff loans during the year amounted to KShs 18,936,207 (2019: KShs 18,073,796).



Notes to the financial statements (Continued)

34. Related party transactions (Continued)

(b) Loans and advances to directors and their associates

The Group has entered into transactions with its directors and their associates as follows:

	2020	2019
	KShs'000	KShs'000
Gross amount at 1 January	707,526	707,250
Interest charged	9,778	3,653
Loans disbursed	-	-
Revaluation	47,271	-
Cash received	-	(3,377)
Net amount at 31 December	<u>764,575</u>	<u>707,526</u>

(c) Related party deposits

Included in deposits is KShs 26,982,000 (2019 – KShs 25,394,000) due to a subsidiary company. Interest paid on these deposits during the year amounted to KShs 560,000 (2019 – KShs 563,000).

(d) Due from Industrial and Commercial Development Corporation (ICDC)

Included in other assets is outstanding balance of payment from the sale of Finance house due from ICDC amounting to KShs 128,587,000(2019 - KShs 189,079,000).

(e) Key management compensation

Compensation to senior management for the year ended 31 December 2020 amounted to KShs 81,965,604 (2019 – KShs 72,576,666).

(f) Directors remuneration

	2020	2019
	KShs'000	KShs'000
Fees for services as a director	1,900	1,500
Other emoluments	15,708	13,453
	<u>17,608</u>	<u>14,953</u>

35. Financial assets that may be pledged or resold by counterparties

As at 31 December 2020, Government securities amounting to KShs 3,856.0 million (2019 – KShs 4,456.0 million) were pledged as security against the facility from the Central Bank of Kenya. These transactions are conducted under terms that are usual and customary to standard lending, and securities borrowing and lending activities.

Notes to the financial statements (Continued)

36. Reserves

(a) Statutory reserves

The statutory reserve represents an appropriation from retained earnings to comply with Central Bank of Kenya's prudential guidelines on impairment of loans and advances. It represents the excess loan provisions as computed in accordance with Central Bank of Kenya's prudential guidelines over the impairment arrived at in accordance with International Financial Reporting Standards.

(b) Other reserves

Other reserves comprise of:

- (i) KShs 281,000 of interest reserve established under a lending agreement between the bank and Industrial & Commercial Development Corporation (ICDC). Under the agreement, part of the interest payable on the loan capital balance was retained as interest reserve and is available for furtherance of the bank's business. The interest reserve is not available for distribution.
- (ii) KShs 594,785,000 (2019 - KShs 744,292,292) revaluation reserves on the equity investment in Kenya Hotel Properties Plc net of related tax.

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