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# DIRECTORS, OFFICERS AND ADMINISTRATION

## DIRECTORS

Kung'u Gatabaki

Chairman

Frank Ireri

Managing Director (Appointed 1 July 2006)

Anne A W Amisabuo

David R Ansell\*

The Permanent Secretary to the Treasury

Paul B M Ngugi

Alternate to the Permanent Secretary to the Treasury

Naftali Mogere

Mary Kimotha M'Mukindia

\* American

## COMPANY SECRETARY

Fiona C Fox

Chunga Associates

7th Floor, Rahimtulla Tower

Upper Hill

P O Box 41968

00100 Nairobi GPO

Walker Kontos Advocates

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## REGISTERED OFFICE

Plot No. LR 209/9054

Rehani House

Kenyatta Avenue/Koinange Street

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00100 Nairobi GPO

## SHARE REGISTRAR

Anne Matu, CPS(K)

Housing Finance Company of Kenya Limited

Rehani House

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P O Box 30088

00100 Nairobi GPO

## BANKERS

Barclays Bank of Kenya Limited

Barclays Plaza

P O Box 46661

00100 Nairobi GPO

## AUDITORS

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00100 Nairobi GPO

Citibank NA

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00100 Nairobi GPO

## PRINCIPAL LEGAL ADVISORS

Napier and Stratton Advocates

Williamson House

4th Ngang Avenue

P O Box 40111

00100 Nairobi GPO

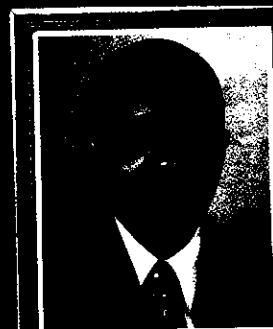
## SUBSIDIARIES

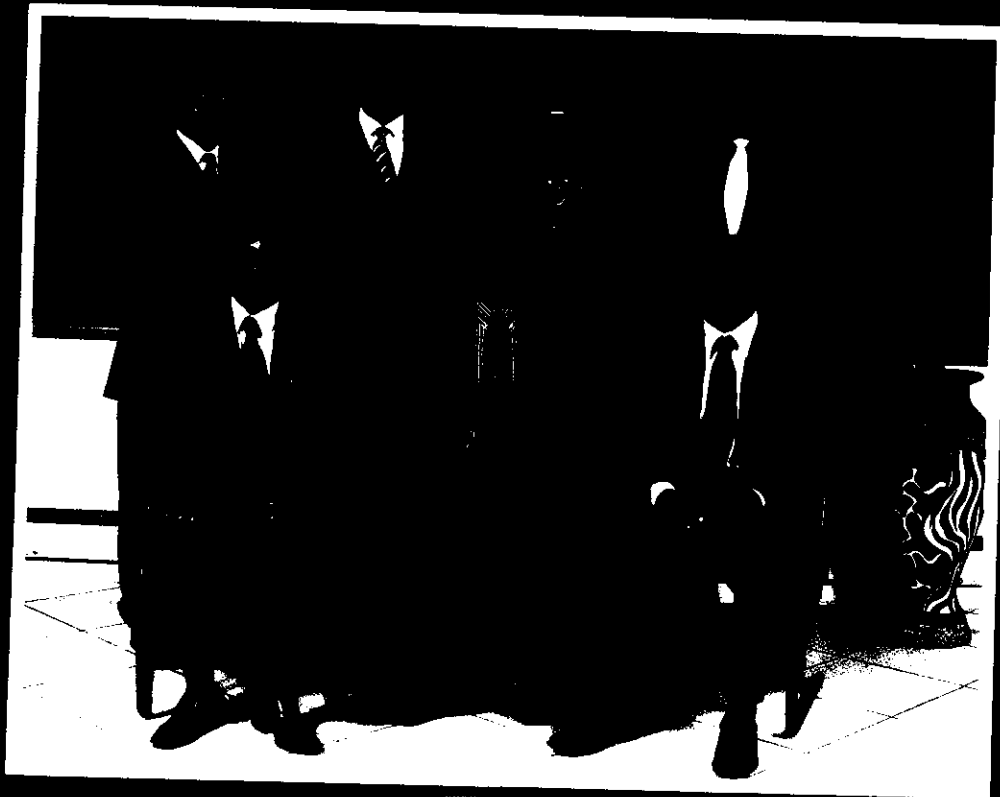
Kenya Building Society Limited

First Permanent (East Africa) Limited



King's Ombaki - Chairman





Back row from left to right

Front row from left to right



# BOARD MEMBERS' PROFILE

## Kung'u Gatabaki

Mr. Gatabaki was appointed Chairman in 2004. He previously worked for 30 years with Actis/CDC (formerly Commonwealth Development Corporation) where he acquired wide experience in project finance, portfolio management and corporate board business. He serves on various company boards including: Chairman of Micra Kenya, Director of Mumias Sugar Co., TPSEA (Serena Hotels), Development Bank of Kenya, Grain Bulk Handlers Ltd., Jacaranda Hotels, Kenya Safari Lodges & Hotels and Shelter Afrique, among others. He studied economics, project finance and management at Legon and Bradford Universities. He is 60 years old and is married with 4 grown up children.

## Frank M Ireri

B Com (Hons), CPA K

Frank Ireri was appointed Managing Director in July 2006. He is a seasoned Banker of 18 years standing and joined from Barclays Bank of Kenya where he was Head of Barclay Card Africa, covering Kenya, Botswana, Zambia, Mauritius, Seychelles and Egypt. Prior to this, he worked with Citibank and Commercial Bank of Africa. During his banking career, he has had international exposure in Poland, Sri Lanka and Zambia.

Mr. Ireri is a Honorary Counsel member of AIESEC and previously held the role of Chairman to the AIESEC Board of Advisors. Between 2001 and 2002 he was also the Chairman of the Kenya Institute of Bankers. He is married with 2 children.

## David R Ansell

BA Mathematics

David Ansell was appointed Director in October 2001. He retired from Citibank in February 2001, after over 30 years of service, including an assignment as Director of Citibank's African businesses based in Nairobi. He was also previously Managing Director of Ecobank Transnational Inc. based in Lome, Togo. He also serves on the Advisory Board of the Private Equity New Markets fund managed by BankInvest, the largest asset Manager in Denmark. He is 61 years old and married with 2 grown up children.

## Naftali O Mogere

Naftali Mogere was appointed Director in July 2004. He was formerly the Managing Trustee of NSSF, and is currently the Managing Director of National Cereals and Produce Board. He has a wide experience in Finance, having served on various company boards including: Consolidated Bank, Bamburi Cement Ltd, EA Portland Cement, National Bank of Kenya, International Board of Social Security - Geneva - for 4 years and Finance and Administration Director in COMESA for 10 years. He was Finance and Administration Director of Preferential Trade Area Reinsurance Company for 10 years and Finance Director/Company Secretary of African Medical Research Foundation (AMREF) for 5 years. He has been the Chief Accountant with Kenya Reinsurance Corporation and Principal Accountant at IDB.

He is member of Kenya Institute of Management (K.I.M.) and the British Institute of Management (B.I.M.). He studied Accounting at University of Nairobi and is a Certified Public Accountant (C.P.A.) and a Certified Public Secretary (C.P.S.). He is married with 5 children.

## Anne A W Amissabuar (Mrs)

LLB, LLM

Mrs Anne Amissabuar was appointed Director in 1995. She is currently a member of the International Bar Association (IBA) Section on Business Law, which includes Banking Law, Section on Legal Practice and on Human Rights. She is also a member of the Private Sector

Corporate Governance Trust (PSCGT), Good Corporate Governance, Member of Federation of Kenya Women Lawyers (FIDA), Director of Institute of Directors (K) and Member of Law Society of Kenya.

## Joseph Kanja Kinyua

MA (Econ)

Mr. Joseph K Kinyua began his career as an Assistant Lecturer at Nairobi University in 1978. He joined the Central Bank of Kenya in 1980 and worked his way through the ranks from an Economist to Director of Research. He also worked as an economist on a fixed term appointment with the International Monetary Fund (IMF) during 1985-1990, after which he returned to the Central Bank of Kenya.

He was appointed Financial Secretary to the Treasury in June 1995, a position he held until July 1999 when he rejoined the Central Bank of Kenya as Director of Financial Markets. In October 2000, he was appointed the Chief Economist of the Central Bank of Kenya and in September 2002, he was appointed the Permanent Secretary to the Treasury, a position he held until January 2003 when he was appointed Permanent Secretary in the Ministry of Planning and National Development. In July 2003, he was appointed Permanent Secretary in the Ministry of Agriculture. He remained there until July 2004, when he was once again appointed Permanent Secretary to the Treasury, where he is currently engaged.

Mr. Kinyua has served as a Director on several Boards of State Corporations. He has also served as a member of the Programme Committee of the African Economic Research Consortium (AERC) and is currently a member of the Board of Governors of AERC and Alternate Governor, World Bank Board of Governors. He holds BA (Econ) and MA (Econ) degrees from Nairobi University.

## Mary Kimotho M'Mukindia (Mrs)

B Com (Hons)

Mary Kimatha M'Mukindia is a Bachelor of Commerce Honors graduate from the University of Nairobi in Kenya and began her career in the Oil Industry, which she has served for over 25 years in various capacities with Exxon Mobil, the Petroleum Institute of East Africa and as an Energy consultant with Enercan. She is currently the Managing Director with the National Oil Corporation of Kenya where she was appointed in April 2003.

Mary is particularly active in Private Sector Organisations, both commercial and charity, and serves on several Boards that include Kenya School of Professional Studies (KSPS), the Petroleum Institute of East Africa (PIEA), the Kenya Petroleum Refineries, Mombasa (KPRL) and Watata Kwanza Trust - a UNICEF initiated charity trust. Mary, who is Vice Chairman of the Kenya member committee to the World Energy Council, was also nominated in February 2005, as the NEPAD liaison for the World Energy Council - Africa Region Committee. In Dec 2006, Mary was conferred a Merit of the Order of the Burning Spear by H.E. The President for her outstanding performance at National Oil and her contribution to the industry as a whole.

Mary has also been involved, and continues to be involved, in various government appointed Task Forces which include, The Petroleum Bill - 2000, The Marine Laws Review Task Force - 2002, The Economic Recovery Strategy - 2003 and The Kenya Energy Sector Development Strategy Task Force, The East Africa Community Private Sector Development Strategy Study - as a steering committee member, and in 2003/2004, the Integrated National Transport Policy Committee.

Mary is married with two young children - a son, Mwenda, 11 years and a daughter, Kui-Makani, 8 years.

# CHAIRMAN'S STATEMENT/TAARIFA YA MWENYEKITI

Dear Members,

It is my pleasure to inform you of another successful year for Housing Finance. We had a very good year in terms of growth of business volumes, management of our cost base, recovery efforts on distressed debts and revival of the operations of our subsidiary companies.

## Performance – 2006

Group profit for the year increased by 56% from Kshs. 90m to Kshs 141m., and the revenue in line with prior years at Kshs. 1,206m. Although we had new business in excess of Kshs. 2 billion, the lowering of mortgage interest rates reduced the overall impact on revenues. The recovery efforts on distressed loans raised Kshs. 1.4 billion. Costs were maintained at prior year levels which demonstrated that the culture of diligent cost management is now engrained in our operations.

## Strategic Direction

Once again my address focuses on the strategic direction of the Company. This year, we have included in this annual report a section by the Managing Director, Mr. Frank Ireri. Frank has already settled in the role and has proved to be a very active member of the Board. One of the key assignments of the Board was to complete a strategy for 2007 – 2011, in line with our tradition of operating under 5 year plans. This has now been done and approved at our Board meeting of February 2007. You will appreciate that the strategy cannot be reproduced here, but I would like to assure you that this Company now has a very aggressive vision and strategy for the next five years. We have developed a work plan that will transform this Company's operations and take profitability to levels unprecedented.

The transformation will depend on several key decisions by you the Shareholder and we the Board on your behalf. This brings me to a very important item that will be an agenda of an EGM this year.

## Capital raising by Rights Issue

Since taking over as Chairman of your Company our objective has been to transform the balance sheet structure to facilitate the business growth that we project. You will have seen an announcement indicating that we had approached the regulators and Capital Markets Authority to approve a rights issue. I would like to emphasize here how important the raising of new capital will be for Housing Finance to fund its growth. As shareholders of this Company, you have the responsibility to ensure that we give the Board and Management the tools they require to enable them to compete and make a better return.



Kung'u Gatabaki – Chairman

Kwa wanachama,

Ni fahari kwangu kuwafahamisha mwaka mwingine wenye ufanisi kwa Housing Finance. Tulikuwa na mwaka mzuri wa ukuaji wa viwango vya biashara, udhibiti wa gharama zetu na juhudi za ukusanyaji wa madeni sumbufulu na pia ufufuzi wa kampuni tanzu.

## Matokeo mwaka 2006.

Faida za kundi mwaka huu ziliongezeka kwa asilimia 56 (56%) kutoka shilingi milioni 90 hodi milioni 141. Mapato yalikuwa sowa na mwaka uliotangulia kwa shilingi milioni 1,206. Ingawa tulikuwa na biashara mpya iliyazolisha shilingi bilioni 2, kupunguka kwa riba iliyatokana na rehani kulipelekea kupunguka kwa mapata. Juhudi za ukusanyaji mikopa tata zililazisha shilingi bilioni 1.4. Gharama zilizidhibitiwa mwaka uliotangulia katika viwango na kudhibitiwa kwamba zaezi hili limesisitizwa kwenye shughuli zetu.

## Mwelekeo wa Mkakati

Kwa mara nyingine, hotuba yangu inaangazia mwelekeo wa mpango wa kampuni ambapo mwaka huu tumehusisha taarifa ya Meneja Mkurugenzi Bw. Frank Ireri katika ripoti ya mwaka. Toyari Frank amechukua wajibu na ni mwanachama mwenye bidii katika halmashauri. Majawapa wa majukumu muhimu ya halmashauri ilikuwa kukamilisha mpango wa utekelezaji kazi wa 2007. Mnatambua kwamba mpango huu hauwezi kutalewa tena hapa lakini nataka kuwahakikishia kwamba kampuni hii kwa sasa ina hima, maana na mpango wa miaka mitano ijayo. Tumeandaa mpango wa maendeleo ambao utabadili shughuli za kampuni na kupelekea faida kupanda hadi viwango visivya na kifani.

Mpango wa kufonya mabadilika utategemea maamuzi fulani muhimu kutaka kwenu wanahisa na sisi wanahalmashauri kwa niaba yenu. Swala hili litakuwa agenda muhimu wakati wa mkutano wa ziada mwaka huu.

## Kupata mtaji kupitia umiliki wa hisa

Tangu nilipachukua hatamu za uenyekiti wa kampuni yenu, lenga letu limekuwa kubadili mizania (balance sheet) ili kuandaa ukuaji wa biashara tunaatazamia. Mtakuwa mmeana tangaza kuashiria kwamba tulikuwa tumetembelea holmoshouri ya soko la hisa (Capital Market Authority-CMA) kuidhinisha swalo la umiliki hisa. Ningependa kusisitiza kambo uzalishaji wa mtaji mpya utakuwa wa Housing Finance ili kugharamio ukuaji wake. Kama wanahisa, mna jukumu la kuhakikisha kwamba mmeipo Holmoshouri na wasimomizi vifao vinavyohitajika kuiwezesha kukabiliana na ushindani kupata matokeo memo.

# CHAIRMAN'S STATEMENT/TAARIFA YA MWENYEKITI (Continued)

## Business Performance & Reorganization

We have reached the stage where our investments in modernizing the Company are putting us in a better competitive position. You are all aware of the Company's journey since the re-branding in 2002, where we set out a program, first to identify talent and create modern internal structures, secondly to improve the products and customer service standards and the third phase was to stimulate growth. We are truly in this third phase and the growth numbers are already serving to reaffirm our position as market leaders for the mortgage business. The second phase on products and customer service required us to match modern or contemporary banking standards meaning a significant investment in technology. You now see the company offering electronic banking solutions and e-banking services, which I hope you are all enjoying through the accounts you opened with us. If you haven't opened an account, please do. It is these investments that are starting to bear fruit and we are committed to sustain and improve the momentum. We have several savers who have been loyal to us even when we offered a more manual service than our competitors, but we believe we have rewarded this loyalty through the better service they are now enjoying. Housing Finance offers a very competitively priced account for savings or transactions, and we are encouraging you to market your institution. The management are monitored in their roles of ensuring growth, but as owners you should be ambassadors of our business.

## Asset Quality and Debt Collection

The ratio of our debts that are in distress in relation to the total portfolio is now very close to industry average, indicating a very impressive performance on the debt recovery front. We have graduated from being classified as an institution that faces difficulties on account of having a low quality book. The growth in new business has also improved the ratio of our good book to bad book, with bad book being a smaller chunk. Collecting distress debt is not an easy assignment and sometimes causes customers to consider us as unsympathetic or inconsiderate. I assure you we offer several different rescue packages for our customers and resort to using our right of sale when all else has not worked. Our Regulators have been directing new policies at us that make it prohibitive on the institution and its capital owners, to keep distress balances in the books. The collection of debt is therefore a critical activity for us. We value our customer and we make every possible alternative to allow them reasonable room to repay their debt. The reduced size of the bad book increases the value of loan repayments that we can take to income.

## Mafanikio ya Biashara na Mpongilio Mpya

Tumefikia hatua ambapo uwekezaji wetu kuimarisha sura ya kampuni yetu unatuweka katika nafasi nzuri ya ushindani. Nyate mwafahamu safari ya kampuni tangu ibuni namba mpya mwaka wa 2002 wakati tulipazindua mpanga, kwanza, kutambua vipawa na kubaresha muundo wa ndani, pili, kuimarisha bidhaa na viwango vya huduma kwa wateja wanaozidi kuongezeka na tatu kuchezea ukuaji. Kwa hakika, tume katika awamu hi ya tatu na ongezeko la wateja linazidi kuthibitisha uongozi wetu katika biashara ya rehani. Awamu ya pili kuhusu bidhaa na huduma kwa wateja ilituhitaji kujihami na mbinu za kisasa za viwango vya benki hivyo kutupelekeo kuwekeza katika teknolojia. Sasa, mnashuhudia benki ikitoa huduma zake kupitia mitambo ya kisasa na e-banking ambayo natumai inawavutia kupitia akaunti mlizafungua nasi. Endapo hujafungua akaunti nasi, tafadhali fanya hivyo. Ni kupitia uwekezaji huu unaoanza kuzaa matunda ambapo tumejitolea kuhimili na kuimarisha. Tuna wateja ambao wamekuwa na imani nasi hata wakati tulipokuwa tukitoka huduma zetu kwo mikono tofauti na washindani wetu. Tunaamini kwamba tumewaridhisha wateja hawa kupitia utoaji wa huduma bara ambazo kwo sasa wanazifurahia. Kampuni ya Housing Finance inakupa huduma nafuu za uwekaji akiba na tunakuhimiza kuvumisha taasisi yako. Wasimamizi wanapigwa darubini kuhusiana na wajibu wao wa kuhakikisha ukuaji lakini kama wamiliki wa kampuni, mnafaa kuwa mobalazi wa biashara yetu.

## Ubora wa Rasimali na ukusanyaji

Uwiano wa madeni sumbufu ikilinganishwa na jumla ya orodha ya fedha zilizowekwa kwa faida sasa zinakaribia kuwa katika kiwango cha wastani na kuashiria mafanikio makubwa ya ukusanyaji madeni. Tumefuzu kutoka kiwango ambapo kampuni ilioradhosheba kama taasisi inayakabiliana na matatizo kwa kutakana na mafanikio ya chini. Ukuaji wa biashara mpya umeimarisha uwiano baina matokea mema na mabaya huku matokea mabaya yakizidi kudidimia. Ukusanyaji wa madeni sumbufu si jamba rahisi na wakati mwingine huwafanya wateja kutuchukulia kama watu wasia na huruma. Ninawahakikishia kwamba, tunawapa wateja wetu njia mbali mbali zo kulipa madeni na kuchukua suluhu la haki yetu kuuza mali endapo mbinu zote hazikufua dafu. Wahakiki wetu wamekuwa wakibuni sera mpya zinazokata taasisi na wamiliki wake kuhifadhi madeni sumbufu kwenye vitabu vyao. Kwa sababu hiya, ukusanyaji madeni ni shughuli muhimu kwetu. Tunadhamini wateja wetu na tunawaandalia mbinu mbali mbali zitakazowawezesha kulipa madeni yao. Kupunguka kwa matokea mabaya kunaimarisha hali ya ulipaji madeni ambayo tunaweza kuchukua kama mapato.

# CHAIRMAN'S STATEMENT/TAARIFA YA MWENYEKITI *(Continued)*

## Subsidiaries

After a long time, our subsidiaries have made a positive contribution to the profit performance. Last year I mentioned that we changed their structure and operations. In the ongoing transformation process we intend to make them active and prominent players in our operations. The development by Kenya Building Society at Kamarock Phase V has been slow but we hope to see the 500 houses put into the market as soon as possible. We have also begun a process to review the arrangement we had made to enable us implement a solution that will deliver the performance we had anticipated.

## Board

We have invited Ms. Beatrice Sabana and Mr. Ken Wathame to join the Board subject to Central Bank of Kenya approval. The nominations and remunerations committee did a thorough review of the needs of the Company and the way in which these individuals matched the skills or experience required. I assure you on behalf of the Board that these individuals are of impeccable character and will bring significant value to Housing Finance, especially at this time of activating our new strategy. I hope you will give them your support.

## Corporate Social Responsibility

We have retained our CSR theme around the improvement of opportunities to people in the informal urban settlements. Although in terms of actual expenditure we are very modest, we have a variety of small but high impact activities we participate in to deliver our theme. Our Managing Director now sits on the Board of Habitat for Humanity, Kenya which serves to take us closer to the underprivileged communities in these informal sectors.

## Dividend

You will recall that when I took over as Chairman of the Company three years ago I promised you that we would be transforming this Company into a profitable and dividend-paying institution. That journey back into profitability and continued dominance of the property market has finally been rewarded. We plan to pay a maiden dividend in respect of our results in 2007. In addition the rights issue gives you a further opportunity to be part of this Company's bright future alongside also the opportunity to trade your rights and realize some cash.

I would like to end there with these brief comments. The Managing Director will brief you on the things he is doing to realize the Company's vision.

Thank you all and God's blessings to you.

Chairman

Kung'u Gatabaki

## Kampuni tanzu

Baada ya muda mrefu, kampuni tanzu zimetaa mchanga maalumu kuhusiana na faida. Mwaka jana nilitaja kwamba tulibadili mfumo na shughuli zake. Kupitia shughuli za sasa za kufanya mabadilika, tunatumai kufanya kampuni hizi kushiriki kikamilifu na kuwa washiriki wakuu katika biashara zetu. Mpanga wa maendeleo wa Kenya Building Society huka Kamarock Phase V umekuwa ukiendelea pale pale lakini tunatumai kuona nyumba 500 zilizajengwa zikiingizwa masakani haraka iwezekanavyo. Pia, tumezindua njia kuchunguza upya mipanga tuliyoandaa kutuwezesha kupata suluhu litakalaleta maendeleo tuliyoandaa.

## Halmashauri

Tumealika Bi. Beatrice Sabana na Bw. Ken Wathame kujiunga na Halmashauri kwa kutegemea idhini kutoka Benki Kuu ya Kenya. Kamati za uteuzi na ujira zilichunguza kwa kina mahitaji ya kampuni na jinsi watu hawa walivyafikiana na elimu au ujuzi uliuhitajika. Kwa niaba ya Halmashauri ninawahakikishia kwamba watu hawa wana sifa nzuri na watailetea Housing Finance manufaa makubwa hasa wakati huu wa kuanzisha mkakati mpya. Natumai kwamba mtawaunga mkana.

## Wajibu wa shirika kwa jamii

Tumedumisha wajibu wetu kwa jamii kwa kuimarisha hali ya maisha ya watu wanaoishi katika makaa yasiya rasmi. Ingawa matumizi yetu ni ya wastani, tuna shughuli ndogo lakini zinazataa athari njema kufanikisha azma yetu. Kwa sasa, Mkurugenzi wetu mkuu anajumuika na halmashauri ya Umaja wa Mataifa inayashughulikia mazingira (Habitat for Humanity, Kenya) inayatuweka karibu na jamii ambazo hazijababatika katika sekta zisizo rasmi.

## Mgao wa faida

Mtakumbuka kwamba nilipachukua hatamu kama mwenyekiti wa kampuni miaka mitatu iliyopita, niliwaahidi kwamba nitabadili hali ya kampuni hii na kuwa taasisi inayaleta faida na kulipa mgao wa faida. Safari ya kuturejesha kupata faida na kuwa wamiliki wa soko la rasimili hatimae imezaa matunda. Tumepanga kutaa mgao wa kwanza wa faida kwa kutegemea matokeo yetu ya 2007. Zaidi na hayo, swala la umiliki wa hisa linakupa fursa kujumuika na kampuni katika ufanisi wa siku za usani na wakati huo kutumia nafasi hiyo kufanya biashara ili kujipatia pesa.

Ningependa kumalizia hapa kwa kutaa vidokezo hivyo vifupi. Meneja Mkurugenzi atawaeleza kuhusu mamba anayafanya kufanikisha ndata ya kampuni.

Asanteni na Mungu awabariki nyate.

Mwenyekiti

Kung'u Gatabaki.

# MANAGING DIRECTORS' REPORT/RIPOTI YA MENEJA MKURUGENZI

It is an honour for me to be presenting to you a report of the Company's performance and prospects going forward. Since joining in July 2006, I have encountered several things which informed me of the enormous brand loyalty that Housing Finance enjoys in this market. I have also had the opportunity to start making the changes I believe will deliver the performance that is expected of me and my team.

## Financial performance 2006

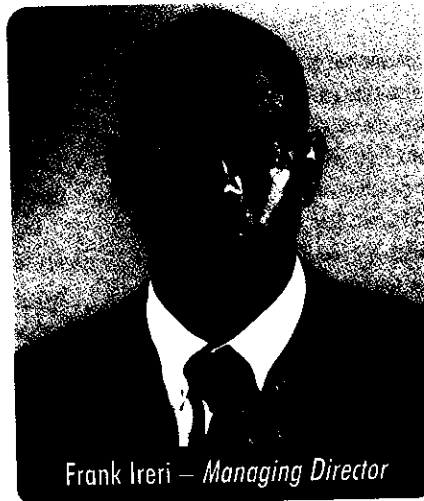
To recap on the 2006 Group performance, we recorded an increase of 56% in profit before tax. This performance was underscored by various factors, first amongst them being that the good book now represents 69% of our net mortgage assets (up from 53% in 2005) whilst our Non performing book represents 31% of our book (down from 47%). This is as a result of the focused and intense debt recovery efforts during the year that resulted in a 35% reduction (KShs 1038m) in the value of our Non performing loans. In addition, our good book grew by 27% and also, we have been able to hold overhead costs at par with prior year, even after the effects of high inflation and volume growth in 2006. This aggressive cost management will continue to be employed even as we look into the future of the Company. Our business and the banking industry in general rely on the acquiring and retaining of good talent and using technology to deliver efficient modern services. We held staff costs at par with prior year which manifests a re-orientation towards aggressively using the investment in technology that has been made so far. We have rolled out several electronic banking products and value-added services that run on our EasyCash debit card. Today our customers can use any of our ATM machines, Kenswitch or PesaPoint ATM machines countrywide and shop anywhere they see the Senator Card sign. We know we offer one of the cheapest savings or transaction accounts for our customers so with such modern functionality and ready access-to-your-cash, we are well positioned to compete with the best.

## Group Company Operations

I also made some changes to the operations of the subsidiaries in the Group. I noted from the past that they made losses and were dampening the overall performance. The new strategy gives them very defined roles and clear objectives for purposes of turning them around and ensuring they positively support our performance. On the Kamarock V development, the situation on the ground is not an encouraging picture of the spirit in which we embarked on the Joint Venture arrangement to see the development completed. We have embarked on instituting very aggressive corrective measures to ensure we bring these houses to the market within an acceptable time frame.

## Staff Development

As we focus on retaining and growing market share, our ability to attract, retain and develop staff plays a key role. We took our staff through various local and overseas courses to enhance their capacity to support our growing business. We are also putting in a lot of effort on leadership development and succession planning.



Frank Ireri — Managing Director

Ni fahari kwangu kuwaletea taarifa ya matokeo na matarajio ya kampuni nyetu.

Tangu nijunge na kampuni hii mwezi Julai, 2006, nimekumbana na mambo mengi yaliyonikumbusha kuhusu imani ambayo kampuni hii imekuwa ikijivunia katika utoaji wa huduma zake. Pia, nimepata nafasi ya kufanya mabadilika ambayo ninaamini yataleta mafanikio yanayotarajiwa kutoka kwangu na timu yangu.

## Matakeo ya kifedha mwaka 2006

Kwa muhtasari tu kuhusu matokeo ya kampuni hii ya 2006, tulikuwa na nyongeza ya faida ya asilimia 56 kabla ya kutozwa ushuru.

Matokeo haya yalitakana na sababu mbali mbali. Kwanza rekodi bora ya matokeo

inasimamia asilimia 69 ya jumla ya rasimali za rehani zetu (ongezeka kutoka asilimia 53 mwaka 2005) huku mikopo yetu ambayo bado haijalipwa ikiwa katika kiwango cha asilimia 31 ambayo imepungua kutoka asilimia 47 mwaka uliatangulia. Matokeo haya yalitakana pia na juhudi za ukusanyaji madeni kwa wakati ufao katika kipindi hiki cha mwaka uliosababisha madeni hayo kupungua kwa asilimia 35 hadi shilingi milioni 1038.

Zaidi ya haya, rehani zetu ziliongezeka kwa 27 huku tukidhibiti gharama za tendakazi hata baada ya kupanda kwa gharama ya maisha kulikaathiri kiwango cha ukuaji cha mwaka wa 2006.

Juhudi hizi za kudhibiti gharama za usimamizi zitaendelea kutumika huku tunapaangazia hali ya baadaye ya kampuni hii.

Shughuli zetu za sekta ya benki kwa ujumla zinategemea wafanyikazi weledi na utumiaji mzuri wa teknolojia kwa ajili ya utoaji huduma bora na za kisasa.

Tulizidhibiti vilivyo gharama zetu huku tukiendelea na uwekezaji katika teknolojia kutokea mwaka uliatangulia hadi mwaka huu.

Mbali na hayo tumezindua mifumo mipya ya benki kupitia mitamba ya elektroniki ambayo imeongeza thamani ya huduma zetu ambazo sasa zinapatikana kupitia kadi zetu za mikopo zilizwazo EasyCash.

Hivi sasa wateja wetu wanaweza kutumia mitamba ya ATM, Kenswitch au PesaPoint kote nchini na kununua bidhaa popote wanapoona namba ya kadi ya Senator.

Tunajua kwamba tunataa majawapo ya huduma nafuu zaidi za uwekaji akiba. Kupitia mifumo hiyo ya kisasa wateja wetu wanaweza kuzifikia haraka pesa zao hivya kutuweka katika nafasi bora ya ushindani na Kampuni zengine.

## Shughuli za kampuni

Nilifanya mabadilika kadhaa ya usimamizi katika kampuni zetu tanzu.

Niligundua kwamba hapo awali kampuni hizi zilikuwa zikipata hasara na kudidimiza matokeo ya jumla.

Mkakati mpya unafanua wazi wazi madhumuni ya mageuzi haya ambayo kwa ujumla ni kuimarisha matokeo yetu.

Katika mradi wa Kamarock V, hali haiidhishi kwani hakuna taswira ya imani ya ushirikiano ambao ulitarajiwa wakati mkataba wa ushirikiano ulipodifiwa.

Hapa tumeanza shughuli za marekebisha ya kimsingi ili kuhakikisha kwamba nyumba hizo zika katika kiwango cha soko kinachakubalika.

# MANAGING DIRECTORS' REPORT/RIPOTI YA MENEJA MKURUGENZI *(Continued)*

## Risk Management

We are all conscious about the dangers unmanaged growth can have on the quality of the asset book. A very strenuous exercise has been run over the last few years with tremendous success to reduce the negative revenue effects we faced when the non performing book was high. We have adapted a very modern and effective risk management structure within the Company to manage all risks we are exposed to. All staff now operate under clear guidelines and approved limits to protect the business from increased exposure. Although the Regulators are also pushing for these improvements, we have designed systems for ourselves that surpass the minimum requirements that the regulator has set.

## Plans for 2007

One of my first assignments was to develop a strategy for the next five years (2007 – 2011). This was completed in consultation with the Board and through the involvement of all the staff of the Company. We have developed a road map that will bring significant change to Housing Finance's position in the property market. We aim to be leaders and as we implement the strategy over the next couple of years, I am confident we shall deliver a financial performance that excels within our chosen industry.

One of the key precedents to the success of this strategy is to inject additional capital into the business. We operate in an industry that is closely regulated by the Central Bank and we have to maintain certain maximum business volumes based on the capital employed. We recently sought approval to have a rights issue and I look forward to your support in making this a success. The Chairman has spoken at length on this in his statement and I ask only that you do heed his call in supporting the rights issue.

On the growth of our two distinct business lines i.e. mobilization of deposits by branch banking and mortgage sales, we have implemented some changes to immediately boost the rate of growth. You will have seen in the media the signing of a mortgage brokerage agreement with AAR, my participation at a conference on investments for the Diaspora and increasing our specialized mortgage services to employers. These activities are opening up new markets for us and giving us product innovation opportunities.

In conclusion, I believe that we have created within the business a desire and a methodology to transform the performance of Housing Finance. Our strong heritage and the important role we play in making property available to Kenyans is well entrenched in the vision and mission of the Company. With my team of managers and staff, we are well on the way to significantly improving our stakeholder value.

Thank you.

Frank Ireri.

## Maendeleo ya wafanyakazi

Huku tunapoangazia kumiliki na kupanua nafasi yetu katika soko, tumewajibika kuwawutia zaidi wafanyakazi kupitia kuimarisha maslahi yaa. Tuliwapa mafunza mbalimbali wafanyakazi wetu hapa nchini na pia ng'ambo ili kuwawezesha kumudu ukuaji wa shughuli zetu. Pia tunahimiza uimarishaji wa maongozi na mipango ya urithi wa nafasi za kazi.

## Kusimamia Hatari

Tunachukua tahadhari kutokana na hatari inayoweza kusababishwa na kutasimamiwa vyema kwa ubora wa rasilimali yetu. Zoezi kali limekuwa likiendeshwa kwa muda wa miaka michache iliyopita na kupelekea ufanisi mkubwa katika kukabiliana na athari ya kutochunguzwa kwa kiini cha matokeo mabaya. Wafanyakazi wote wanafanya kazi chini ya maongozi yaliyo wazi na ambayo yamekadiriwa vilivyo ili kutoziweka shughuli zetu katika hatari ya kuigwa.

Tumezindua mpanga wa kisasa wa usimamizi katika kampuni ili kuweka viwango vya juu zaidi ya vile vilivyowekwa na wasimamizi wa sekta hii.

## Mipango kwa mwaka wa 2007

Mojawapo wa majukumu yangu ya kwanza, ilikuwa ni kuandaa mpango wa utekelezaji kazi wa miaka 5 (2007-2011). Mpanga huu ulikamilika kwa ushirikiano na halmshauri na kuwahusisha wafanyakazi wote wa kampuni. Tumeandaa mpango ambao utaitolea Kampuni hii ya Housing Finance mabadiliko katika soko la rasilimali. Tunalenga kuwa viangozi. Wakati tunapaandaa mikakati ya miaka kadhaa ijayo, ninao uhakika kwamba tutakuwa na matokeo bora ya kifedha ambayo yatakuwa kielelezo bara cha ufanisi katika nyanja hii.

Mojawapo wa njia muhimu za kufanikisha mpango huu ni kuongeza mtaji katika biashara. Tunatekeleza biashara yetu katika soko ambalo linachunguzwa kwa karibu na Benki Kuu na tunahitajika kudhibiti viwango fulani vya biashara vinavyotegemea mtaji uliawekwa. Hivi karibuni, tuliomba idhini ya swala la uuzaji wa hisa zetu kwa umma na nataraji mtaniunga mkano ili kufanikisha lengo hili. Mwenyekiti amezunguza kwa mapana kuhusu swala hili kupitia taarifa yake na nawaamba kumuunga mkono katika swala hilo la toleo la hisa.

Kuhusu ukuaji wa maeneo mawili muhimu ya biashara zetu, ambayo ni kuhamisha dhamana kupitia uwekaji fedha katika matawi ya benki na uuzaji wa nyumba za rehani, tumefanya mabadiliko kwa lengo la kuimarisha mara moja kiwango cha ukuaji.

Vyombo vya habari vitatoa taarifa kuhusu makubaliano na AAR, na pia kuangazia kushiriki kwangu katika mkutano wa uwekezaji katika eneo hili pamoja na kuongeza huduma zetu maalumu za rehani kwa wajiiri.

Shughuli hizo zote zinafungua masoko mapya kwetu na kutupatia nafasi za kubuni huduma mpya mpya.

Kwa kutamatisha, naamini kwamba tumeanzisha utaratibu utakaoimarisha vilivyo shughuli zetu za ukuaji wa rehani za nyumba. Turathi yetu na wajibu wetu wa kutoa nafasi kwa wakenya kumiliki mali vimefafanuliwa vyema kupitia ruwaza na wita wa kampuni yetu.

Kwa ushirikiano na wasimamizi wenzangu pamoja na wafanyakazi tuka katika mwelekeo wa kuimarisha thamani ya washika dau wetu.

Asanteni

Frank Ireri

# THE DIRECTORS' REPORT

## FDR THE YEAR ENDED 31 DECEMBER 2006

The directors have pleasure in submitting their report, together with the audited financial statements for the year ended 31 December 2006.

### 1 Principal activities

The company is licensed to operate as a mortgage finance institution under the Banking Act (Cap. 488) and seeks to encourage and promote the flow of both private and public savings into financing property ownership.

The subsidiaries' principal activities are development and selling of residential houses and letting of residential houses.

### 2 Results and appropriations

	2006 Kshs'000	2005 Kshs'000
<b>Gross income</b>	<b>1,206,389</b>	<b>1,199,205</b>
<b>Profit/(Loss) before taxation</b>		
Housing Finance Company of Kenya Limited	126,749	101,725
Kenya Building Society Limited	4,932	(10,888)
First Permanent (East Africa) Limited	9,555	(349)
<b>Group profit before taxation</b>	<b>141,236</b>	<b>90,488</b>
<b>Taxation</b>	<b>(40,187)</b>	<b>(31,689)</b>
<b>Profit after taxation</b>	<b>101,049</b>	<b>58,799</b>
<b>Retained profit brought forward</b>	<b>137,579</b>	<b>368,042</b>
	<b>238,628</b>	<b>426,841</b>
<b>Dividends — proposed</b>	<b>-</b>	<b>-</b>
<b>Transfer to statutory reserve</b>	<b>(127,882)</b>	<b>(289,262)</b>
<b>Retained profit carried forward</b>	<b>110,746</b>	<b>137,579</b>

### 3 Dividend

The directors do not recommend the payment of a dividend (2005 — Nil).

### 4 Directors

The directors who served during the year are set out on page 3.

### 5 Auditors

The auditors, KPMG Kenya, have indicated their willingness to continue in office in accordance with Section 159(2) of the Kenyan Companies Act (Cap. 486) and subject to Section 24(1) of the Banking Act (Cap. 488).

### 6 Approval of financial statements

The financial statements set out on pages 17 to 41 were approved at a meeting of Directors held on 8 March 2007.

## BY ORDER OF THE BOARD

Company Secretary

Date: 8 March 2007

# TAARIFA YA WAKURUGENZI

## YA MWAKA UNAOISHA TAREHE 31 DESEMBA 2006

Wakurugenzi wanafuraha kutaa ripati yao pamoja na taarifa ya uhasibu iliyokaguliwa kwa kipindi cha mwaka uliamalizikia Desemba 31, 2006.

### 1 Shughuli muhimu

Kampuni imepewa leseni kuendesha shughuli za utaji mkopa wa ujenzi wa nyumba chini ya sheria za benki (kifungu 488) na imejitalea kushinikiza na kusaidia uwekaji Akiba kwa watu binafsi na umma ili kugharamia ujenzi wa makao. Shughuli nyingine ndogo ni pamoja na kustawisha uuzaji wa nyumba za kuishi.

### 2 Matokeo na Matumizi

	2006 Kshs'000	2005 Kshs'000
<b>Mapato ya Jumla</b>	<b>1,206,389</b>	<b>1,199,205</b>
<b>Faida/(Hasara) kabla ya ushuru</b>		
Housing Finance Company of Kenya Ltd	120,719	101,725
Kenya Building Society Limited	1,117	(10,888)
First Permanent (East Africa) Limited	955	(349)
<b>Faida ya kampuni kabla ya ushuru</b>	<b>122,791</b>	<b>90,488</b>
<b>Ushuru</b>	<b>(90,134)</b>	<b>(31,689)</b>
<b>Faida baada ya ushuru</b>	<b>32,657</b>	<b>58,799</b>
<b>Jumla ya faida iliyowasilishwa</b>	<b>117,579</b>	<b>368,042</b>
	<b>110,928</b>	<b>426,841</b>
<b>Mgao wa faida uliipendekezwa</b>		
Pesa zilizohifadhiwa kisheria	(127,882)	(289,262)
<b>Faida iliyowasilishwa</b>	<b>110,746</b>	<b>137,579</b>

### 3 Mgao wa faida

Wakurugenzi hawapendekezi malipo ya mgao wa faida (2006- sufuri)

### 4 Wakurugenzi

Wakurugenzi waliohudumu mwaka huu wameangaziwa katika ukurasa wa tatu.

### 5 Wahasibu

Wakaguzi wa hesabu, KPMG Kenya wameonyesha nia yao ya kutaka kuendelea na jukumu hili kwa mujibu wa kifungu nambari 159(2) sheria za makampuni za Kenya (aya ya 486) na kwa mujibu wa sehemu ya 24 (1) ya sheria za benki (aya 488).

### 6 Kuidhinishwa kwa taarifa ya matumizi ya pesa

Taarifa kuhusu matumizi ya fedha zilizoko ukurasa wa 17 hadi 41 ziliidhinishwa wakati wa mkutano wa wakurugenzi uliofanyika 8 Machi 2007.

## KWA AMRI YA HALMASHAURI

Katibu wa Kampuni

Imenukuliwa: 8 Machi 2007

# CORPORATE GOVERNANCE

The company is committed to the standards of Corporate Governance. The following disclosures aim at emphasizing this commitment.

## 1 Role of the Board

The Board is responsible for drawing and implementing strategies for the long-term success of the company as well as carrying out the fiduciary duty of monitoring and overseeing the activities of management. Continuous performance measurement is the key towards ensuring that shareholders' value is maximized. In so doing the Board holds regular meetings to discuss performance and chart the way forward for the company. Notices and agenda for all Board meetings are circulated to all Directors on a timely basis together with the respective documents for discussion.

## 2 Composition of the Board

The Board is composed of five non-executive Directors in addition to the chairman. Mr. Frank Ireri is the Managing Director. All the non-executive Directors are considered to be independent of management influence and do not engage in any business or interest that could impair their participation in the management of the company.

## 3 Re-election and resignation of Directors

All the non-executive Directors are required to submit themselves for re-election every three years. The Managing Director's performance is measured continuously in line with the company's performance management framework. Any impending resignation of Directors and the underlying circumstances are disclosed in the annual report.

## 4 Board and Management Committees

The Board has constituted sub-committees chaired by either Non-Executive Directors or the Executive Director to assist it in the discharge of its role of identifying the current and future business risks while ensuring that the necessary systems and controls are in place to enable such risks to be monitored and effectively managed. The key board Committees include:

### Board Strategic Review Committee

This is composed of two non-executive Directors, the Managing Director, Director of Business Development and Director of Finance. The Non Executive Directors are:

- Kung'u Gatabaki (Chairman)
- Mary Kimatha M'Mukindia

The committee's responsibilities include:

- providing direction and oversight on the bank's strategic initiatives
- obtaining external professional advice as and when deemed necessary

### Board Audit and Risk Committee

This is composed of four non-executive Directors:

- David Ansell (Chairman)
- Paul Ngugi
- Mary Kimatha M'Mukindia
- Naftali Mogere

The Board audit and risk committee is responsible for assisting the Board to discharge its corporate governance responsibilities as follows:

- Relationship with and independence of the external auditors;
- Reliability and appropriateness of the disclosures in the financial statements and other external financial communication;
- Implementation of an effective business risk management framework;
- Ensuring compliance with internal controls;

### Nomination and Remuneration Committee

This is a Board Committee comprising of three non-executive Directors. The Chief Executive is an ex officio member. The three non-executive Directors are:

- Kung'u Gatabaki
- Mary Kimotho M'Mukindia
- Anne Amisobuar

The Committee's responsibilities are in particular to consider matters related to the proposing of new nominees for the Board, assessing the performance and effectiveness of the Board of Directors, the Chief Executive Officer and Senior Management as well as managing the recruitment and the appointment of the Executive Director and Senior Management.

During the year, five scheduled board meetings were convened for which the attendances by Directors were as shown below:

- Kung'u Gatabaki, David Ansell and Frank Ireri (Appointed 1 July 2006) attended all meetings.
- Anne Amisobuar and Mary Kimatho M'Mukindia attended four meetings.
- Naftali Mogere and The Permanent Secretary to the Treasury attended three meetings.

The review and evaluation of the board and its committees for the year shall be completed by 31 March 2007.

# CORPORATE GOVERNANCE *(Continued)*

## 4 Board and Management Committees *(Continued)*

### Credit Committee

This is a Board Committee comprising of four Non-Executive Directors. The committee's main function is to sanction all applications for large loans. The four Non-Executive Directors are:

- David Ansell (Chairman)
- Naftali Mogere
- Mary Kimatha M'Mukindia
- Anne Ammissabour

A number of Management committees have been established by the Board to oversee operations in some critical areas. These are:

- Executive committee (EXCD)
- Asset and Liability committee
- Risk Management committee
- Lending committee
- Arrears Management committee
- Information Technology Steering committee

The Board appoints other committees as and when the necessity arises.

## 5 Internal audit function

The group has a fully operational internal audit function that is led by a senior member of staff. The function is responsible for evaluating business and operating risks and internal controls put in place to mitigate the risks. It is also responsible for supervising documentation and reviews of the Company policies and procedures.

## 6 Communication with shareholders

The Company is committed to:

- Ensuring that shareholders and the financial markets are provided with full and timely information about its performance
- Compliance with regulations and obligations applicable to the Stock Exchange and the Capital Markets Authority

Information is distributed to the shareholders through an annual report and press notices following the release of quarterly, half yearly and annual results. Press releases are also produced whenever there are significant developments to report on.

## 7 Directors' benefits and loans

All the non-executive Directors have continued to receive Directors' fees. The aggregate amount of Directors' fees is disclosed in Note 7 to the financial statements.

## 8 Major shareholders as at 31 December 2006

	<b>Name of the Shareholder</b>	<b>No of shares</b>	<b>%age shareholding</b>
1	CDC Group PLC	28,635,000	24.90
2	National Social Security Fund	11,899,001	10.35
3	Government of Kenya	8,422,850	7.32
4	Narthbaund Holdings Ltd	4,236,136	3.68
5	Steel Son Ltd	3,850,268	3.35
6	Nomura Nominees Ltd – A/C JMM	3,621,026	3.15
7	The Mbari Security Company Ltd	3,605,491	3.14
8	Nairobi Modern Feeds Ltd	1,666,238	1.45
9	Kibuwa Enterprises Ltd	1,095,929	0.95
10	Kibutu George Nganga	440,445	0.38
	<b>TOTAL</b>	<b>67,472,384</b>	<b>58.67</b>

## 9 Distribution of shareholders as at 31 December 2006

<b>Shareholder (Number of shares)</b>	<b>No. of shareholders</b>	<b>No. of shares held</b>	<b>% shareholding</b>
1-500	8,354	2,261,398	1.97
501-5,000	4,293	3,747,808	3.26
5,001-10,000	12,083	28,815,067	25.06
10,001-100,000	347	6,803,347	5.92
100,001-1,000,000	27	1,886,786	1.64
Over 1,000,000	26	71,485,594	62.15
<b>TOTAL</b>	<b>25,130</b>	<b>115,000,000</b>	<b>100</b>

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Kenyan Companies Act requires the directors to prepare financial statements for each financial year, which give a true and fair view of the state of affairs of the group and the company as at the end of each financial year and of the operating results of the group for that year. It also requires the Directors to ensure that the company keeps proper accounting records, which disclose with reasonable accuracy the financial position of the group. They are also responsible for designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error, selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances. The directors are also responsible for safeguarding the assets of the group and company.

The directors accept responsibility for the financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgments and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act. The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the group and company and of the group operating results.

The directors further accept responsibility for the maintenance of accounting records which may be relied upon in the preparation of financial statements, as well as adequate systems of internal financial control.

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

Directors:

Kung'u Gatabaki

David R. Ansell

Frank Ireri

**Date: 8 March 2007**

## TAARIFA KUHUSU WAJIBU WA WAKURUGENZI

Sheria za Kenya kuhusu makampuni zinawahitaji wakurugenzi kuandaa ripoti ya uhasibu itakayafafanua na kutaa mwangaza kuhusiana na shughuli za kundi na kampuni kwa kipindi chote cha mwaka uliamalizika. Sheria hizi zinawahitaji wakurugenzi kuhakikisha kwamba kampuni limehifadhi vyema rekodi zao za hesabu ambazo zitafichua hali halisi ya kifedha. Pia, wanahitajika kuchukua jukumu la kulinda rasilimali za kundi na kampuni.

Wakurugenzi hukubali kuchukua jukumu la taarifa ya ukaguzi wa pesa ambayo imeandaliwa kwa kufuata sera za uhasibu ambazo zimefanywa uhakiki na makisia yanayafaa kwa kufungamana na viwango vya kimataifa na, kwa mujibu unaahitajika katika sheria za makampuni za Kenya. Wakurugenzi wanakubaliana kwa kauli moja kwamba, taarifa ya ukaguzi wa pesa inataa hali halisi kuhusiana na maswala ya kifedha na matakea ya shughuli za kundi na kampuni.

Zaidi ya haya, wakurugenzi hukubali kuchukua jukumu la kudumisha rekodi za ukaguzi wa pesa zinazoweza kutegemewa wakati wa kuandaa taarifa ya hesabu pamoja na taratibu zinazafaa kudhibiti ukaguzi wa kila siku wa fedha.

Hakuna ishara zazote zilizajitokeza kuvutia hisia za wakurugenzi kuonyesha kwamba, kampuni na washirika wake watasitisha shughuli zao kwa kipindi cha miezi kumi na mbili ijaya kuanzia siku ya kutalewa kwa taarifa hii.

Wakurugenzi:

Kung'u Gatabaki

David R. Ansell

Frank Ireri

**Tarehe: 8 Machi 2007**

# INDEPENDENT AUDITORS' REPORT

TO THE MEMBERS OF HOUSING FINANCE COMPANY OF KENYA LIMITED

We have audited the group financial statements of Housing Finance Company of Kenya Limited set out on pages 17 to 41 which comprise of the balance sheets of the group and the company at 31 December 2006, and the group's income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

**Directors' responsibility for the financial statements**

As stated on page 15, the directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error, selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

**Auditor's responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Opinion**

In our opinion, the financial statements give a true and fair view of the financial position of the group and the company at 31 December 2006, and the group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the Kenyan Companies Act.

**Report on other legal requirements**

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

- We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purpose of our audit.
- In our opinion, proper books of account have been kept by the company, so far as appears from our examination of those books; and
- The balance sheet of the company is in agreement with the books of account.

**KPMG KENYA**  
**CERTIFIED PUBLIC ACCOUNTANTS**  
**PO BOX 40612**  
**NAIROBI**  
**8 March 2007**

# RIPOTI YA WAHASIBU WA KUJITEGEMEA

KWA WANACHAMA WA HOUSING FINANCE COMPANY OF KENYA LIMITED

Tumeandaa taarifa kuhusu matumizi ya pesa ya Housing Finance Company kwa kipindi cha mwaka uliomalizika Desemba 31, 2006 kama ilivyoanyeshwa kupitia kurasa za 17 hadi 41 na kujumuisha pamoja mizania (Balance Sheet) ya kampuni, mapato ya kundi, taarifa kuhusu mabadiliko ya ulinganifu na mapata halisi ya kampuni kwa kipindi cha mwaka kilichomalizika, na muhtasari wa vipengele muhimu vya sera za uhasibu miangoni mwa vidokezo vingine.

**Wajibu wa wakurugenzi kuhusiana na maoni ya matumizi ya pesa**  
Kama ilivyoaeleza kupitia ukurasa wa 15, wakurugenzi wanajukumu la kuandaa na kutaa taarifa iliya sawa ya matumizi haya ya pesa kwa mujibu wa viwango vya kimataifa. Wajibu huu unahusu, kuandaa, kubuni, kuanzisha na kudumisha maingizo ya fedha ambaya yatatumika kuandaa taarifa ya fedha isiya danganyifu iwe ni kwa hila au makosa; kutenga na kutumia sera zinazohitajika za uhasibu na kutaa makadirio ya pesa ya maana.

**Wajibu wa ukaguzi wa pesa**

Wajibu wetu ni kutoa maoni kuhusu na taarifa hii ya matumizi ya pesa kwa mujibu wa ukaguzi wetu. Tulifanya ukaguzi kwa mujibu wa viwango vya kimataifa vya uhasibu. Viwango hivyo vinatuhitaji kuzingatia maadili, kupanga na kutekeleza ukaguzi wa pesa ili kupata uhakika wa maana kwamba, taarifa ya ukaguzi haina udanganyifu wowote.

Ukaguzi wa pesa unahusu uzingatiaji wa hatua kupata ushahidi wa idadi na fichuzi katika taarifa ya matumizi ya pesa. Hatua zilizoteuliwa zinategemewa uamuzi wetu ikiwema kukadiria hatari ya udanganyifu katika taarifa iwe ni kutokana na hila au makosa. Wakati wa ukadiriaji huo, tunazingatia ukaguzi wa ndani unaohusiana na maandalizi ya taarifa ya haki ya matumizi ya pesa ili kubuni taratibu za ukaguzi wa pesa zinazohitajika lakini si kwa kutoa maoni kuhusiana na sera za uhasibu zilizatumika na makadirio ya maana ya uhasibu yaliyoandaliwa na wasimamizi pamoja kukadiria mtazamo kamili wa taarifa ya pesa.

Tunaamini kwamba ushahidi kuhusu ukaguzi wa pesa tuliopata unatosha na unaafaa kutupatia msingi wa mooni yetu.

**Maoni**

Kwa maoni yetu, taarifa kuhusu matumizi ya pesa inatoa mtazamo wa kweli na halisi wa kifedha wa Kampuni kufikia Desemba 31, 2006 na mapato halisi kwa kipindi hicho cha mwaka, kwa mujibu wa viwango vya kimataifa vya ukaguzi wa pesa na sheria makampuni za Kenya.

**Ripoti kuhusu mahitaji mengine ya kisheria**

Kufungamana na kifungu cha sheria za makampuni cha Kenya kuhusiana na ripoti tunayatoa, kwa mujibu wa ukaguzi wetu wa hesabu, kwamba;

- Tumeepata maelezo na fafanzu zinazohitajika ambazo kwa ujuzi na imani yetu zilikuwa muhimu wakati wa kufanya ukaguzi wetu.
- Kwa maoni yetu, kampuni imehifadhi vyema rekodi ya vitabu vya hesabu kama inavyodhihirika kutokana na uchunguzi wetu wa vitabu hivyo na;
- Mizania (balance sheet) ya kampuni inakwenda sambamba na rekodi ya vitabu vya hesabu.

**KPMG KENYA**  
**KAMPUNI YA WAHASIBU**  
**S.L.P 40612**  
**NAIROBI**  
**Tarehe: 8 Machi 2007**

# CONSOLIDATED PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31 DECEMBER 2006

	Note	2006 KShs'000	2005 KShs'000
INTEREST INCOME	3	1,023,357	1,016,927
INTEREST EXPENSE	4	(349,042)	(353,380)
NET INTEREST INCOME		674,315 ✓	663,547
IMPAIRMENT LOSSES ON MORTGAGE ADVANCES	13(b)	(104,284)	(138,681)
NET INTEREST INCOME AFTER IMPAIRMENT		570,031	524,866
LOSSES ON MORTGAGE ADVANCES TO CUSTOMERS		183,032 ✓	182,278
NON INTEREST INCOME	5	(611,827)	(616,656)
NON INTEREST EXPENSES	6	141,236	90,488
PROFIT BEFORE TAXATION	7	(40,187)	(31,689)
TAXATION	8	101,049	58,799
NET PROFIT AFTER TAX		KShs 0.88	KShs 0.51
BASIC AND DILUTED EARNINGS PER SHARE	9	-	-
DIVIDENDS PER SHARE	10	-	-

The notes set out on pages 22 to 41 form an integral part of these financial statements.

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# CONSOLIDATED BALANCE SHEET

AT 31 DECEMBER 2006

	Note	2006 KShs'000	2005 KShs'000
<b>ASSETS</b>			
Cash and bank balances	11(a)	129,415	182,530
Placements with other banks	11(b)	1,015,611	1,780,471
Investment in Government Securities	12	896,754	796,196
Mortgage advances to customers (Net)	13(a)	6,345,349	6,443,855
Non current assets held for sale	16		16,165
Other assets	17	114,593	88,967
Housing Development Projects	18	9,430	9,430
Property and equipment	19(a)	302,090	302,090
Prepaid operating lease rentals	20	54,739	54,739
Intangible assets	21	62,595	62,595
Deferred tax asset	22(a)	57,743	57,743
Tax recoverable		46,413	46,413
Defined benefit asset	23	19,884	19,884
<b>TOTAL ASSETS</b>		<b>9,861,078</b>	<b>9,861,078</b>
<b>LIABILITIES</b>			
Customers' deposits	24	8,433,503	8,433,503
Other liabilities	25	155,861	155,861
Deferred tax liability	22(a)	-	-
		<b>8,589,364</b>	<b>8,589,364</b>
<b>SHAREHOLDERS' EQUITY (Page 23)</b>			
Share capital	26	575,000	575,000
Reserves		645,964	645,964
Shareholders' income notes and loans	27	50,750	50,750
		<b>1,271,714</b>	<b>1,271,714</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>9,861,078</b>	<b>9,861,078</b>

The financial statements set on pages 17 to 41 were approved by the Board of Directors on 8 March 2007 and were signed on its behalf by:

Directors:

Kung'u Gatabaki

David R. Ansell

Frank Ireri

Company Secretary

Fiana C Fax

The notes set out on pages 22 to 41 form an integral part of these financial statements.

# COMPANY BALANCE SHEET

AT 31 DECEMBER 2006

	Note	2006 KShs'000	2005 KShs'000
<b>ASSETS</b>			
Cash and bank balances	11(a)	179,425	182,455
Placement with other banks	11(b)	1,015,618	1,780,471
Investment in Government Securities	12	896,754	796,196
Mortgage advances to customers (Net)	13(a)	6,345,349	6,443,855
Investment in subsidiaries	14	130,020	130,020
Dividend receivable		-	15,000
Non current assets held for sale	16	-	16,165
Other assets	17	85,166	86,675
Property and equipment	19(b)	330,893	295,639
Prepaid operating lease rentals	20	43,556	44,064
Intangible assets	21	49,299	62,595
Deferred tax Asset	22(b)	-	3,945
Tax recoverable		13,458	25,888
Defined benefit asset	23	51,967	19,884
<b>TOTAL ASSETS</b>		<b>9,141,505</b>	<b>9,902,852</b>
<b>LIABILITIES</b>			
Customers' deposits	24	7,619,250	8,437,315
Amounts due to subsidiary company	15	18,259	23,789
Other liabilities	25	126,103	150,760
Deferred tax liability	22(b)	10,217	-
		<b>7,773,829</b>	<b>8,611,864</b>
<b>SHAREHOLDERS' EQUITY (Page 23)</b>			
Share capital	26	575,000	575,000
Reserves		741,926	665,238
Shareholders' income notes and loans	27	50,750	50,750
		<b>1,367,676</b>	<b>1,290,988</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>9,141,505</b>	<b>9,902,852</b>

The financial statements set on pages 17 to 41 were approved by the Board of Directors on 8 March 2007 and were signed on its behalf by:

Directors:

Kung'u Gatabaki

David R. Ansell

Frank Ireri

Company Secretary

Fiana C Fox

The notes set out on pages 22 to 41 form an integral part of these financial statements.

# CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2006

		2006	2005
	Note	Ksh'000	Ksh'000
<b>Net cash flows from operating activities</b>	<b>28(a)</b>	<u>(494,597)</u>	<u>975,766</u>
<b>INVESTING ACTIVITIES</b>			
Purchase of property and equipment		(66,585)	(6,530)
Proceeds from sale of prepaid operating lease rentals		23,823	-
Proceeds from sale of property and equipment		24,542	696
Additions to intangible assets		<u>(7,376)</u>	<u>(2,583)</u>
<b>Net cash flow from investing activities</b>		<u>(25,596)</u>	<u>(8,417)</u>
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>28(b)</b>	<u>(520,193)</u>	<u>967,349</u>

The notes set out on pages 22 to 41 form an integral part of these financial statements.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2006

	Share capital Kshs'000	Revaluation reserve Kshs'000	Share premium Kshs'000	Statutory reserve Kshs'000	Retained profits Kshs'000	Total Kshs'000
At 1 January 2005	575,000	100,429	25,705	-	368,042	1,069,176
Net profit after taxation	-	-	-	-	58,799	58,799
Revaluation surplus on property and equipment	-	92,989	-	-	-	92,989
Transfer to statutory reserve	-	-	-	289,262	(289,262)	-
At 31 December 2005	575,000	193,418	25,705	289,262	137,579	1,220,964
Net profit after taxation	-	-	-	-	101,049	101,049
Transfer to statutory reserve	-	-	-	127,882	(127,882)	-
At 31 December 2006	575,000	193,418	25,705	417,144	110,746	1,322,013

The notes set out on pages 22 to 41 form an integral part of these financial statements.

# COMPANY STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2006

	Share capital Kshs'000	Revaluation reserve Kshs'000	Share premium Kshs'000	Statutory reserve Kshs'000	Retained profits Kshs'000	Total Kshs'000
At 1 January 2005	575,000	100,429	25,705	-	378,750	1,079,884
Net profit after taxation	-	-	-	-	67,365	67,365
Revaluation surplus on property and equipment	-	92,989	-	-	-	92,989
Transfer to statutory reserve	-	-	-	289,262	(289,262)	-
At 31 December 2005	575,000	193,418	25,705	289,262	156,853	1,240,238
Net profit after taxation	-	-	-	-	76,688	76,688
Transfer to statutory reserve	-	-	-	127,882	(127,882)	-
At 31 December 2006	575,000	193,418	25,705	417,144	105,659	1,316,926

The notes set out on pages 22 to 41 form an integral part of these financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

## FOR THE YEAR ENDED 31 DECEMBER 2006

### 1 SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below:

#### (a) Basis of preparation

The consolidated financial statements are prepared in accordance with and comply with International Financial Reporting Standards. The financial statements are prepared under the historical cost convention as modified by the revaluation of certain items of property and equipment. Available for sale financial assets and financial liabilities held at fair value through income statement are stated at fair value.

The preparation of financial statements in conformity with International Financial Reporting Standards requires management to make judgement, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. The estimates and assumptions are based on the Directors' best knowledge of current events, actions historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about the carrying values of assets and liabilities are not readily apparent from other sources. Actual results may differ from these estimates.

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

#### (b) Consolidation principles

The consolidated financial statements comprise the financial statements of the parent company and its subsidiaries made up to 31 December 2006. Subsidiaries are entities controlled by the company. Control exists when the company has power, directly or indirectly, to govern the financial and operating policies so as to obtain benefits from its activities. In assessing control, potential voting right that presently are exercisable are taken into account. A listing of the subsidiaries is set out on page 30 (Note 14).

#### (c) Revenue recognition

Income is recognised on an accrual basis in the period in which it is earned.

##### (i) **Interest income and expense**

Interest income and interest expense are recognised on an accrued basis taking into account the effective interest rate of the interest earning assets and interest bearing liabilities.

##### (ii) **Fees and commission**

Fees and commission income is recognised when the service is provided.

#### (d) Foreign currencies

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

These consolidated financial statements are presented in Kenya shillings (KShs), which is the company's functional currency. Items included in the financial statements are measured using the currency of primary economic environment in which the entity operates i.e Kenya shillings

##### (ii) **Foreign currency transactions**

Transactions in foreign currencies during the year are converted into Kenya Shillings at the rates ruling at the transaction dates. Assets and liabilities at the balance sheet date which are expressed in foreign currencies are translated into Kenya shillings at rates ruling at the balance sheet date. The resulting realised and unrealised differences from conversion and translations are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currency are recorded at the exchange rate ruling at the date of the transaction.

#### (e) Property and equipment

Freehold land and buildings and buildings on leasehold land are included in the financial statements at their historical cost or amount at any subsequent valuation less accumulated depreciation and impairment losses.

Freehold land is not depreciated.

Depreciation is calculated on a straight line basis to allocate the cost or revalued amount to their residual values over their estimated useful lives as follows:-

Computers	20%
Motor vehicles	20%
Office equipment, fixtures and fittings	5% - 20%

Buildings on leasehold land are depreciated over the remaining period of the lease. Buildings on freehold land are depreciated over fifty years.

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

## (e) Property and equipment (Continued)

Excess depreciation is the difference between the depreciation charge for the year based on the revalued amount and the original cost of the related property and equipment. On an annual basis, the amount relating to the excess depreciation is transferred from revaluation reserves to retained earnings to recognise the use of the property and equipment.

The residual value, if not insignificant is reassessed annually.

## (f) Intangible assets

Where computer software is not an integral part of the related computer hardware it is recognised as an intangible asset. The software are stated on the balance sheet at costs less accumulated amortisation and impairment losses.

Software costs are amortised over five (5) years on a straight line basis from the date they are available for use.

## (g) Prepaid operating lease rentals

Leases where a significant portion of the risks and rewards of ownership are retained by the lessor, are classified as operating leases. Payments made under operating leases arrangements (whether pre-paid or past-paid) are charged to the income statement on a straight-line basis over the period of the lease.

## (h) Employee benefits

### (i) Defined Benefit Scheme

The group operates a funded defined benefit plan for all permanent employees. The group's net obligation is calculated by estimating the amount of future benefits due to employees in relation to their service in current and prior periods. The fair value of plan assets is deducted to obtain the net obligation. The calculation is carried out by an independent Actuary every three years based on the projected unit credit method.

Where the calculation results in a benefit to the group, the recognised asset is limited to the net total of any unrecognised actuarial losses and past service costs, and the present value of any future refunds from the plan; or reduction in future contributions to the plan. Actuarial gains and losses are charged to the income statement over the average remaining working lives of employees participating in the scheme. The company's contribution in respect of retirement benefit costs are charged to the income statement in the year to which they relate.

The benefits are paid to the retiring staff in accordance with the scheme rules.

### (ii) Employee Share Ownership Plan (ESOP)

Approval to establish an ESOP was given by the shareholders on 26 July 2006. No further steps have been taken to operationalise the Plan.

### (iii) Accrued leave

Accrual for annual leave is made as employees earn it and reduced when taken.

## (i) Taxation

Tax on the operating results for the year comprises the current charge and change in deferred tax. Current tax is provided on the results in the year as shown in the financial statements adjusted in accordance with tax legislation.

Deferred tax is provided using the balance sheet liability method on all temporary differences between the carrying amounts for financial reporting purposes and the amounts used for taxation purposes, except differences relating to the initial recognition of assets and liabilities which affect neither accounting nor taxable profit.

Deferred tax is calculated on the basis of the tax rates currently enacted.

Deferred tax assets relating to the carry forward of unused tax losses are recognized to the extent that future taxable profit is expected to be available against which the unused tax losses can be utilized.

Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

## (j) Cash and cash equivalents

For the purpose of presentation of cash flows in the consolidated financial statements, the cash and cash equivalents include cash in hand and at bank, net balances with banking institutions and investment in government securities with a maturity period within three months from date of acquisition.

## (k) Financial assets

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

# NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

## (k) Financial assets *(Continued)*

### (i) **Financial assets at fair value through profit or loss**

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

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

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

### (iii) **Held-to-maturity**

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

### (iv) **Available-for-sale**

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates or exchange rates. Purchases and sales of financial assets at fair value through profit or loss, held to maturity and available for sale are recognised on trade-date the date on which the Group commits to purchase or sell the asset. Loans are recognised when cash is advanced to the borrowers. Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method. Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity should be recognised in profit or loss. However, interest calculated using the effective interest method is recognised in the income statement.

## (l)

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

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

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

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

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and advances. Interest on the impaired asset continues to be recognised through the unwinding of the discount.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 19. PROPERTY AND EQUIPMENT

#### a) Group:

	Freehold land KShs'000	Buildings KShs'000	Furniture, fixtures, equipment & motor vehicles KShs'000	Total KShs'000
<b>Cost or valuation:</b>				
At 1 January 2006	7,000	233,651	389,495	630,146
Additions	-	-	66,585	66,585
Disposals	-	-	(21,357)	(21,357)
At 31 December 2006	7,000	233,651	434,723	675,374
<b>Comprising:</b>				
At cost	-	20,651	434,723	455,374
At valuation	7,000	213,000	-	220,000
	7,000	233,651	434,723	675,374
<b>Depreciation:</b>				
At 1 January 2006	-	3,148	324,908	328,056
Charge for the year	-	3,265	26,803	30,068
Disposals	-	-	(20,019)	(20,019)
At 31 December 2006	-	6,413	331,692	338,105
<b>Net book value:</b>				
At 31 December 2006	7,000	227,238	103,031	337,269
At 31 December 2005	7,000	230,503	64,587	302,090

The Group's land and buildings were professionally valued by the Group's valuer on an open market basis on 31 December 2005. The resulting surplus was credited to revaluation reserve.

The net book value (NBV) of properties at their historical cost is as follows:

	2006 KShs 000	2005 KShs '000
Freehold land	206	206
Buildings	50,907	53,109

Included in property and equipment are assets with a gross value of KShs 240,594,359 (2005 – KShs 219,629,047) which are fully depreciated and still in use. Such assets would have attracted a notional depreciation of KShs 40,749,184 (2005 – KShs 38,664,629).

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

19. **Property, plant and equipment** (Continued)

**b) Company:**

	Freehold land KShs'000	Buildings KShs'000	Furniture, fixtures, equipment & motor vehicles KShs'000	Total KShs'000
<b>Cost or valuation:</b>				
At 1 January 2006	7,000	225,055	384,129	616,184
Additions	-	-	66,585	66,585
Disposals	-	-	(21,357)	(21,357)
At 31 December 2006	7,000	225,055	429,357	661,412
<b>Comprising:</b>				
At cost	-	12,055	429,357	441,412
At valuation	7,000	213,000	-	220,000
	7,000	225,055	429,357	661,412
<b>Depreciation:</b>				
At 1 January 2006	-	1,003	319,542	320,545
Charge for the year	-	3,190	26,803	29,993
Disposals	-	-	( 20,019)	( 20,019)
At 31 December 2006	-	4,193	326,326	330,519
<b>Net book value:</b>				
At 31 December 2006	7,000	220,862	103,031	330,893
At 31 December 2005	7,000	224,052	64,587	295,639

The company's land and buildings were professionally valued by the Group's valuer on an open market basis on 31 December 2005. The resulting surplus was credited to revaluation reserve.

The net book value (NBV) of properties at their historical cost is as follows:

	2006 KShs '000	2005 KShs '000
Freehold land	-	206
Buildings	53,109	53,109

Included in property and equipment are assets with a gross value of KShs 233,225,055 (2005 – KShs 219,629,047) which are fully depreciated and still in use. Such assets would have attracted a notional depreciation of KShs 40,012,254 (2005 – KShs 38,664,629).

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 20. PREPAID OPERATING LEASE RENTALS

	2006		2005	
	Group KShs'000	Company KShs'000	Group KShs'000	Company KShs'000
<b>Cost:</b>				
At 1 January	57,932	45,706	60,332	48,106
Disposals in the year	(3,320)	-	-	-
Transfer to non current assets held for sale	-	-	(2,400)	(2,400)
	<u>54,612</u>	<u>45,706</u>	<u>57,932</u>	<u>45,706</u>
<b>Amortisation:</b>				
At 1 January	3,193	1,642	2,868	1,440
Charge for the year	690	508	657	534
Transfer to non current assets held for sale	-	-	(332)	(332)
Disposals	(459)	-	-	-
	<u>3,424</u>	<u>2,150</u>	<u>3,193</u>	<u>1,642</u>
<b>At 31 December</b>	<b><u>51,188</u></b>	<b><u>43,556</u></b>	<b><u>54,739</u></b>	<b><u>44,064</u></b>

As at 31 December 2006 the un-expired lease period ranges from 67 to 89 years.

### 21. INTANGIBLE ASSETS

	2006 KShs'000	2005 KShs'000
<b>Group and Company</b>		
<b>Software costs</b>		
At January	114,499	112,429
Additions during the year	7,376	2,583
Reclassification	-	(513)
	<u>121,875</u>	<u>114,499</u>
<b>Amortisation</b>		
At January	51,904	31,427
Amortisation during the year	<u>20,672</u>	<u>20,477</u>
As at 31 December	<u>72,576</u>	<u>51,904</u>
<b>Net book value as at 31 December</b>	<b><u>49,299</u></b>	<b><u>62,595</u></b>

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

## 22. DEFERRED TAX ASSET

### a) Group

Movements in deferred tax assets and liabilities are as follows:

	01.01.2006 KShs '000	Recognised in income KShs'000	31.12.2006 KShs'000
<b>Arising from:</b>			
Plant and equipment	777	92	869
Other general provisions	(385)	(270)	(655)
General provision on mortgages	(10,424)	4,716	(5,708)
Defined benefit asset	5,965	9,625	15,590
Tax losses carried forward	(53,676)	1,213	(52,463)
<b>Net deferred tax</b>	<b>(57,743)</b>	<b>15,376</b>	<b>(42,367)</b>
<b>Comprising:</b>			
Deferred tax asset	<b>57,743</b>	-	<b>52,584</b>
Deferred tax liability	-	-	<b>10,217</b>
<b>b) Company</b>			
<b>Arising from:</b>			
Plant and equipment	744	91	834
Other general provisions	(230)	(270)	(499)
General provision on mortgages	(10,424)	4,716	(5,708)
Defined benefit asset	5,965	9,625	15,590
	<b>(3,945)</b>	<b>14,162</b>	<b>10,217</b>

## 23. EMPLOYEE BENEFITS

### (a) Retirement benefits asset

#### Group and Company

An actuarial valuation was undertaken as at 31 December 2006 and the previous one was at 31 December 2003 is shown below:

	31.12.2006 KShs'000	31.12.2003 KShs'000
Present value of funded obligations	350,754	239,655
Fair value of scheme assets	(466,833)	(278,682)
Net under funding in the scheme	(116,079)	(39,027)
Unrecognised actuarial loss	64,112	19,143
<b>Net asset in the balance sheet</b>	<b>(51,967)</b>	<b>(19,884)</b>
Movements in the net asset recognised in the balance sheet are as follows:		
Net (asset)/ liability at 1 January 2004 and 2003	(19,884)	22,281
Net expense recognised in the income statement	32,083	14,742
Employer contributions	(64,166)	(56,907)
<b>Net asset in the balance sheet at 31 December</b>	<b>(51,967)</b>	<b>(19,884)</b>
The expense recognised in the income statement is as follows:		
Current service costs	45,741	14,774
Interest on obligation	71,533	18,467
Expected return on plan assets	(85,191)	(18,499)
<b>Total expense included in administration expenses</b>	<b>32,083</b>	<b>14,742</b>
Discount rate (p.a.)	9%	9%
Expected return on scheme assets (p.a.)	9%	9%
Future salary increases (p.a.)	7%	7%
Future pension increases (p.a.)	0%	0%

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

## 23. EMPLOYEE BENEFITS (Continued)

### (a) Retirement benefits asset (Continued)

Historical information	2006 KShs'000	2005 KShs'000	2004 KShs'000	2003 KShs'000	2002 KShs'000
Present value of funded obligations	350,754	297,187	250,358	239,655	205,019
Fair value of scheme assets	466,833	365,091	291,635	273,037	185,880
Net under funding in funded plan	(116,079)	(67,904)	(41,277)	(33,382)	19,139
Unrecognised actuarial gain/(loss)	64,112	28,938	14,004	13,498	-
Net liability in the balance sheet	(51,967)	(38,966)	(27,273)	(19,884)	19,139

The group expects to pay KShs 23,945,000 in contributions to the defined benefit plan in 2007.

### (b) Employee Share Option Plan (ESOP)

During the year an Employee Share Ownership Plan (ESOP) was to be set up which is to facilitate the ownership of shares in Housing Finance by employees of the company. The approval of the establishment of the ESOP was given by the shareholders on 26 July 2006 and no further steps have been taken to operationalise the Plan.

## 24. CUSTOMERS' DEPOSITS

	2006		2005	
	Group KShs'000	Company KShs'000	Group KShs'000	Company KShs'000
<b>Government and parastatals:</b>				
Payable within 90 days	348,210	348,210	345,751	345,751
Payable after 90 days and within one year	109,054	109,054	9,279	9,279
Payable after one year	799,814	799,814	1,019,159	1,019,159
<b>Private sector and individuals:</b>				
Payable within 90 days	2,674,653	2,675,180	5,579,487	5,583,299
Payable after 90 days and within one year	3,313,131	3,313,131	845,134	845,134
Payable after one year	373,861	373,861	634,693	634,693
	<u>7,618,723</u>	<u>7,619,250</u>	<u>8,433,503</u>	<u>8,437,315</u>

(a) Included in customers' deposits is KShs 527,488 (2005 – KShs 3,811,533) due to a subsidiary, Kenya Building Society Limited.

(b) The weighted average effective interest rate on customer deposits as at 31 December 2006 was 3.70% (2005 – 4.85%).

## 25. OTHER LIABILITIES

	2006		2005	
	Group KShs'000	Company KShs'000	Group KShs'000	Company KShs'000
The Government of Kenya – exchange risk assumption fees	-	-	125	125
Interest payable on the Government of Kenya Income Notes	2,093	2,093	2,093	2,093
House sales deposits	1,564	-	2,203	-
Project costs accruals	2,467	-	2,799	-
Withholding tax payable	9,959	9,959	11,675	11,675
Other liabilities	116,045	114,051	136,966	136,867
	<u>132,128</u>	<u>126,103</u>	<u>155,861</u>	<u>150,760</u>

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

26.

Group and Company	2006 KShs'000	2005 KShs'000
<b>Authorised, issued and fully paid</b>		
115,000,000 Ordinary shares at KShs 5.00 each	575,000	575,000

The holders of ordinary shares are entitled to receive dividends declared from time to time and are entitled to one vote per share at annual and general meetings of the company.

27. **GOVERNMENT OF KENYA INCOME NOTES AND LOANS**

Group and Company	2006 KShs'000	2005 KShs'000
Government of Kenya — Income Notes	50,750	50,750

The Government of Kenya — Income Notes carry no redemption date and is charged interest at a fixed rate of 8.25% per annum (2005 — 8.25%).

28. **RECONCILIATION OF CASH FLOW STATEMENT**

a) <b>Reconciliation of operating profit to net cash flows from operating activities</b>	2006 KShs'000	2005 KShs'000
Group profit before taxation		90,488
Depreciation		25,697
Amortisation of intangible asset		20,477
Amortisation of prepaid operating lease rentals		657
Profit on sale of prepaid operating lease rentals		-
Intangible asset expensed		513
Profit on sale of non-current asset held for sale, property and equipment		(674)
(Decrease)/increase in customer deposits		371,312
Net movement in mortgage advances to customers		139,186
Investment in Government securities		200,109
(Increase)/decrease in other assets		250,877
Decrease in other liabilities		(122,654)
Increase in defined benefits assets		-
Increase in housing projects		(222)
<b>Net cash flows from operating activities before tax</b>	<b>(486,127)</b>	<b>975,766</b>
Tax paid		-
<b>Net cash flows from operating activities</b>	<b>(486,127)</b>	<b>975,766</b>
<b>b) Analyses of cash and cash equivalents</b>		<b>Change in the year</b>
	<b>2006</b>	<b>2005</b>
	<b>KShs'000</b>	<b>KShs'000</b>
Cash in hand and bank	182,530	( 3,075)
Balances due from banking institutions	1,780,471	(764,853)
Investment in government securities	100,000	247,735
	<b>2,063,001</b>	<b>(520,193)</b>

29.

(a) The company is the defendant in a law suit claiming damages for breach of contract.

(b) As at 31 December 2006, the company had issued guarantees in the ordinary course of business to third parties amounting to KShs 6.59 million (2005 — KShs 1.26 million).

## NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

### 30. OPERATING LEASE ARRANGEMENTS

#### **Group and company**

#### **The bank as a lessor**

Rental income earned during the year was KShs 21,673,706 (2005 – KShs 19,300,793). At the balance sheet date, the bank had contracted with tenants for the following future lease receivables:

	2006 KShs'000	2005 KShs'000
Within one year	10,536	3,266
In second to fifth year inclusive	26,552	29,937
After five years	34,245	19,904
	<u>71,333</u>	<u>53,107</u>

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

#### **The bank as a lessee**

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

Within one year	491	1,537
In second to fifth year inclusive	13,202	14,920
After five years	13,401	10,033
	<u>27,094</u>	<u>26,490</u>

Operating lease payments represent rentals payable by the bank for its office premises. Leases are negotiated for an average term of 6 years.

### 31. MORTGAGE COMMITMENTS

#### **Group and Company**

Mortgage commitments amounting to KShs 1,245,085,000 (2005 – KShs 727,940,000) are analysed below:

Commitment in principle but not authorised for payment	566,685	305,528
Authorised but not paid	678,400	422,412
	<u>1,245,085</u>	<u>727,940</u>

### 32. CAPITAL COMMITMENTS

#### **Group and Company**

Authorised but not contracted	<u>84,848</u>	<u>135,884</u>
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### 33. ASSETS PLEDGED AS SECURITY

As at 31 December 2006, there were no assets pledged by the group to secure liabilities and there were no secured group liabilities.

## NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

### 34. RELATED PARTY TRANSACTIONS

#### Group and Company

The group has entered into transactions with its employees as follows:

<b>(a) Loans</b>	<b>2006 KShs'000</b>	<b>2005 KShs'000</b>
At 1 January	157,287	139,972
Loans advanced during the year	57,196	47,300
Reclassified third party loans	(1,036)	(15,639)
Loans repayments received	(33,799)	(14,346)
<b>At 31 December</b>	<b>179,648</b>	<b>157,287</b>
<b>Comprising:</b>		
Mortgage advances	145,314	120,632
Staff car loans	33,293	33,320
Other	1,041	3,335
<b>At 31 December</b>	<b>179,648</b>	<b>157,287</b>

Included in the related party are staff car loans of KShs 33,293,212 (2005 – KShs 33,320,058). The related interest income in 2006 was KShs 18,071,141 (2005 – KShs 9,784,782).

In the normal course of business, transactions have been entered with certain related parties at commercial terms.

**(b)** Remuneration to directors is disclosed under Note 7.

### 35. CAPITAL MANAGEMENT

The Central Bank of Kenya sets and monitors capital requirements for banks and other non-bank financial institutions. In implementing the current capital requirements Central Bank of Kenya requires the company to maintain a prescribed ratio of total risk weighted assets. This requirement is calculated for market risk in the banking portfolio of Housing Finance.

The regulatory capital is analysed in two tiers:

- Tier 1 capital includes ordinary share capital, share premium, perpetual bonds, retained earnings, translation reserve and minority interest after deduction of 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 includes qualifying subordinated liabilities, collective impairment allowances and the element of the fair value reserves relating to unrealized gains on equity instruments classified as available for sale.

The company'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 company recognizes 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 company and its individually regulated operations have complied with all externally imposed capital requirements throughout the period. There has been no material changes in the group's management of capital during the period.

The company's regulatory capital position as at 31st December was as follows.

# NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

## 35. CAPITAL MANAGEMENT *(Continued)*

	2006 KShs'000	2005 KShs'000
<b>Tier 1 capital</b>		
Ordinary share capital	575,000	575,000
Share premium	25,705	25,705
Retained earnings	105,659	156,853
	<u>706,364</u>	<u>757,558</u>
<b>Tier 2 capital</b>		
Collective allowances for impairment	67,411	289,262
Qualifying subordinated liabilities	99,105	99,105
	<u>166,516</u>	<u>388,367</u>
<b>Total regulatory capital</b>	<u>872,880</u>	<u>1,145,925</u>
<b>Risk weighted assets</b>		
<b>Capital ratios</b>	<b>2006</b>	<b>2005</b>
Total regulatory capital expressed as a percentage of total risk-weighted assets	16.19%	15.83%
Total tier 1 capital expressed as a Percentage of risk-weighted assets	13.10%	10.47%

## 36. RISK MANAGEMENT

This section provides details of the group's exposure to risk and describes the methods used by management to control risk. The most important types of financial risks to which the group is exposed are credit risk, liquidity risk and market risk mainly interest risk.

### (i) Credit risk

The group is subject to credit risk through its lending and investing activities.

The group's primary exposure to credit risk arises through its mortgage advances to customers. The amount of credit exposure in this regard is represented by the carrying amounts of the assets on the balance sheet. The group is also exposed to credit risk on debt investments. The current credit exposure in respect of the instruments is equal to the carrying amount of these assets in the balance sheet.

The risk that counterparties to instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the group deals with counterparties of good credit standings and obtain collateral. An assessment of the extent to which fair values of collaterals cover existing non performing mortgage advances is highlighted in Note 13 (c) of these financial statements.

The group also monitors concentration of credit risk that arise by customer in relation to mortgage advances to customers. The group has no significant exposure to any individual customer or counterparty.

### (ii) Liquidity risk

Liquidity risk arises in the general funding of the group's activities. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

The group has access to a diverse funding base. Funds are raised mainly from deposits and share capital. This enhances funding flexibility, limits dependence on any one source of funds and generally lowers the cost of funds. The group strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with a range of maturities. The group continually assesses liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall company strategy.

In addition the group holds a portfolio of liquid assets as part of its liquidity risk management strategy.

### (iii) Interest rate risk

The group's operations are subject to the risk of interest rate fluctuations to the extent that interest earning assets and interest bearing liabilities mature or reprice at different times or in differing amounts. Risk management activities are aimed at optimizing net interest income; given market interest rates levels consistent with the group's business strategies. The group does not have any significant interest rate risk exposures.

# NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

## 36. RISK MANAGEMENT *(Continued)*

### *(iv) Operational risk*

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

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

### *Risk measurement and control*

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

## 37. FINANCIAL INSTRUMENTS

### *Liquidity risk*

### *Contractual maturity analysis of assets and liabilities*

The table below analyses the liquidity position of the group's financial assets and liabilities;

	Due on Demand KShs'000	Due within 3 months KShs'000	Due between 3 and 12 months KShs'000	Due between 1 and 5 years KShs'000	Due after 5 years KShs'000	Total KShs'000
<b>Assets</b>						
Cash and bank balances	76,067	103,388	-	-	-	179,455
Placements with other banks	300,000	715,618	-	-	-	1,015,618
Investment in Government securities	-	347,735	79,019	470,000	-	896,754
Net mortgage advances to customers	-	432,904	314,763	1,149,864	4,447,818	6,345,349
Other assets	-	1,041	113,552	-	-	114,593
Housing development projects	-	-	-	9,683	-	9,683
Property and equipment	-	-	-	-	337,269	337,269
Prepaid operating lease rentals	-	-	-	-	51,188	51,188
Intangible Assets	-	-	-	-	49,299	49,299
Deferred tax	-	-	-	-	52,584	52,584
Taxation	-	-	-	-	30,072	30,072
Retirement benefit asset	-	-	-	-	51,967	51,967
<b>Total</b>	<b>376,067</b>	<b>1,600,686</b>	<b>507,334</b>	<b>1,629,547</b>	<b>5,020,197</b>	<b>9,133,831</b>
<b>Liabilities, shareholders' funds, loans and income notes</b>						
Customer deposits	165,873	2,856,990	3,422,185	1,119,071	54,604	7,618,723
Other liabilities	-	15,283	116,845	-	-	132,128
Deferred tax liability	-	-	-	-	10,217	10,217
Share capital	-	-	-	-	575,000	575,000
Reserves	-	-	-	-	747,013	747,013
Shareholders' income notes	-	-	-	-	50,750	50,750
<b>Total</b>	<b>165,873</b>	<b>2,872,273</b>	<b>3,539,030</b>	<b>1,119,071</b>	<b>1,437,584</b>	<b>9,133,831</b>
<b>Net liquidity gap</b>	<b>210,194</b>	<b>(1,271,587)</b>	<b>(3,031,696)</b>	<b>510,476</b>	<b>3,582,613</b>	<b>-</b>
<b>At 31 December 2005</b>						
Total assets	980,974	1,723,020	255,046	1,719,863	5,182,175	9,861,078
Total Liabilities and Equity	302,499	5,639,430	993,582	191,114	2,734,453	9,861,078
<b>Net liquidity gap</b>	<b>678,475</b>	<b>(3,916,410)</b>	<b>(738,536)</b>	<b>1,528,749</b>	<b>2,447,722</b>	<b>-</b>

Customer deposits on demand relate mostly to savings accounts and short notice time deposits. Although classified in this band, previous experience has shown that customers do not generally withdraw significant amounts and are therefore of a long term nature.

## NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

### (l) Identification and measurement of impairment of financial assets *(Continued)*

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

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

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

### (m) Impairment for non-financial assets

The carrying amounts of the Group's non-financial assets, other than investment property and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the assets' recoverable amount is estimated. The recoverable amount of goodwill is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro-rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

### (n) Segmental reporting

Segment information is presented in respect of the group's business segments, which is the primary format and is based on the nature of products and services which the group offers. The group has no distinguishable geographical segments.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Inter-segment pricing is determined on an arms length basis.

### (a) 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.

### (p) Earnings per share

Earnings per share are calculated based on the profit attributable to shareholders divided by the number of ordinary shares. Diluted earnings per share is the same as the basic earnings per share. Diluted earnings per share are computed using the weighted average number of equity shares and dilutive potential ordinary shares outstanding during the year. During the year there were no outstanding shares with dilutive potential.

### (q) 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.

### (r) Offsetting

Financial assets and liabilities are offset and the net amount reported on the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

### (s) New standards and interpretations not yet adopted

FRS 7 Financial Instruments: Disclosures and the Amendment to IAS 1 Presentation of Financial Statements Capital Disclosure: requires extensive disclosures about the significance of financial instruments for an entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. IFRS 7 and amended IAS 1, which become mandatory for the group's 2007 financial statements will require extensive additional disclosures with respect to group; financial instruments and share capital.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

2.

	Mortgage business KShs'000	House sales KShs'000	Other KShs'000	Eliminations KShs'000	Total 2006 KShs'000	Total 2005 KShs'000
Gross revenue (external)	1,196,524	-	14,291	(4,426)	1,206,389	1,199,205
Segment profit/(loss) before tax	126,749	4,932	13,981	(4,426)	141,236	90,488
Taxation	(35,062)	(1,213)	(3,912)	-	(40,187)	(31,689)
Segment profit/(loss) after tax	91,687	3,719	10,069	(4,426)	101,049	58,799
Other information:						
Segment assets	9,141,505	110,927	42,129	(160,730)	9,133,831	9,861,078
Segment liabilities	7,773,829	5,405	8,101	(26,267)	7,761,068	8,589,364
Depreciation/amortisation expense	(51,105)	(325)	-	-	(51,430)	(46,831)
Capital expenditure	73,961	-	-	-	73,961	6,530

3.

	2005 Ksh'000
Advances to customers	865,864
Treasury bills	4,408
Treasury bonds	43,712
Placements with other banks	102,943
	1,016,927

4.

Customer deposits	349,194
Interest on borrowed funds	4,186
	353,380

5.

Fees and commission income	37,806
Rental income	19,301
Other operating income	124,497
Gain on sale of investment property, property and equipment and prepaid operating lease rentals	674
	182,278

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 6. NON INTEREST EXPENSES

	2006 Ksh'000	2005 Ksh'000
Salaries and employee benefits	326,736	360,869
Rental expenses	23,331	20,313
Deposit Protection Fund	12,155	12,139
General administration expenses	249,605	223,335
	<u>611,827</u>	<u>616,656</u>

The following items are included with salaries and employee benefits:

Compulsory social welfare contributions	521	552
Contributions to the defined benefit retirement scheme	27,265	25,082
Increase in the defined benefit scheme asset (Note 23(a))	(32,083)	-
<b>Total</b>	<u>( 4,297)</u>	<u>25,634</u>

The average number of employees engaged by the company during the year was 214 (2005-229).

	2006	2005
Management	133	136
Unionisable	74	83
Contractual	6	9
Temporary	1	1
<b>Total</b>	<u>214</u>	<u>229</u>

Included in salaries and employees benefits are contributions to the defined benefits retirement scheme for employees. During the year, the group made contributions of KShs 27,786,305 (2005 – KShs 21,188,485)

### 7. PROFIT BEFORE TAXATION

The profit before taxation is arrived at after charging/(crediting):

	2006 Ksh'000	2005 Ksh'000
Directors' remuneration:		
- Fees	1,990	1,750
- Expenses	1,700	2,812
- As executives	10,095	24,677
Auditors' remuneration	5,446	4,976
Amortisation of prepaid operating lease rentals	690	657
Amortisation of intangible assets	20,672	20,477
Depreciation	30,068	25,697
Profit on sale of property and equipment, leasehold land and non-current assets held for sale	<u>(28,001)</u>	<u>(674)</u>

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

## 8. TAXATION

	2006 Ksh'000	2005 Ksh'000
Current tax at 30%	21,811	31,246
Deferred tax charge (Note 22(a))	15,376	443
	<u>40,187</u>	<u>31,689</u>

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

	2006 Ksh'000	2005 Ksh'000
Accounting profit before taxation	141,236	90,488
Tax at the applicable corporation tax rate of 30%	42,371	27,146
Utilisation of unrecognised tax losses brought forward	(287)	-
Tax effect of non-deductible costs and non-taxable income	(1,897)	4,543
	<u>40,187</u>	<u>31,689</u>

## 9. EARNINGS PER SHARE

### Basic

Earnings per share are calculated based on the profit attributable to shareholders divided by the number of ordinary shares in issue in each period as follows.

	2006 Ksh'000	2005 Ksh'000
Net profit for the year attributable to shareholders	101,049	58,799
Number of ordinary shares in issue (in thousands)	115,000	115,000
Basic earnings per share	KShs 0.88	KShs 0.51
Diluted earnings per share	KShs 0.88	KShs 0.51

## 10. DIVIDEND PER SHARE

### Dividends

	2006	2005
Number of ordinary shares in issue (in thousands)	115,000	115,000
Dividends per share	KShs. 0.00	KShs. 0.00

## 11. (a) CASH AND BANK BALANCES

	2006		2005	
	Group KShs'000	Company KShs'000	Group KShs'000	Company KShs'000
Cash at hand	76,067	76,067	50,503	50,443
Current account balances	103,388	103,358	132,027	132,012
	<u>179,455</u>	<u>179,425</u>	<u>182,530</u>	<u>182,455</u>

## b) PLACEMENTS WITH OTHER BANKS

	2006 KShs'000	2005 KShs'000
Group and Company		
Due within 90 days	<u>1,015,618</u>	<u>1,780,471</u>

The weighted average effective interest rate on placement with other banks as at 31 December 2006 was 6.63% (2005 – 8.31%).

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 12. INVESTMENT IN GOVERNMENT SECURITIES

Group and Company	2006 KShs'000	2005 KShs'000
<b>Held to Maturity</b>		
Treasury bills due within 90 days	347,735	100,000
Treasury bands due within 90 days	-	153,080
Treasury bonds due within 180 days	9,019	1,290
Treasury bands due after 180 days	540,000	541,826
	<u>549,019</u>	<u>696,196</u>
	<u>896,754</u>	<u>796,196</u>

The weighted average effective interest rate on government securities as at 31 December 2006 was 6.30% (2005 – 6.31%).

### 13. MORTGAGE ADVANCES TO CUSTOMERS

#### a) Group and Company

Mortgages	8,331,178	9,876,465
Less: Provision for impairment losses	(1,985,829)	(3,432,610)
	<u>6,345,349</u>	<u>6,443,855</u>
<b>Maturing:</b>		
Within five years	1,897,531	2,205,144
Over five years to ten years	2,701,108	2,678,273
Over ten years to fifteen years	1,669,006	1,360,590
Over fifteen years	77,704	199,848
	<u>6,345,349</u>	<u>6,443,855</u>

#### b) Reserve for Impairment losses

	Impairment losses KShs'000	Portfolio impairment KShs'000	Total KShs'000
<b>At 1 January 2005</b>	<b>4,250,820</b>	<b>31,347</b>	<b>4,282,167</b>
Impairment made in the year	153,577	(14,896)	138,681
Written off against balance	(988,238)	-	(988,238)
<b>At 31 December 2005</b>	<b>3,416,159</b>	<b>16,451</b>	<b>3,432,610</b>
Impairment made in the year	101,707	2,577	104,284
Written off against balance	(1,551,065)	-	(1,551,065)
<b>At 31 December 2006</b>	<b>1,966,801</b>	<b>19,028</b>	<b>1,985,829</b>

#### c) Mortgage advances

Mortgage advances include an amount of KShs 1,965,682,000 (2005 – KShs 3,003,936,000) net of impairment losses, which have been classified as impaired mortgages. The estimated realisable value of securities held against this net balance is KShs 3,065,848,100 (2005 – KShs. 4,174,249,000).

	2006 KShs'000	2005 KShs'000
Interest on impaired mortgages which has not yet been received in cash	<u>1,924,062</u>	<u>3,515,854</u>

The weighted average effective interest rate on mortgage advances to customers as at 31 December 2006 was 14.11% (2005 – 13.35%).

# NOTES TO THE FINANCIAL STATEMENTS *(Continued)*

## 14. INVESTMENT IN SUBSIDIARIES

		2006 Ksh'000	2005 Ksh'000
	<b>Shareholding</b>		
Kenya Building Society Limited	100%	125,000	125,000
First Permanent (East Africa) Limited	100%	5,020	5,020
		<u>130,020</u>	<u>130,020</u>

## 15. AMOUNTS DUE TO SUBSIDIARIES

### Company:

First Permanent (East Africa) Limited	<u>18,259</u>	<u>23,789</u>
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## 16. NON CURRENT ASSETS HELD FOR RESALE

### Group and Company

#### Cost or valuation:

At 1 January 2006	17,400	-
Transfer from property and equipment		15,000
Transfer from prepaid lease rentals		2,400
Disposed during the year	(17,400)	-
At 31 December 2006	<u>17,400</u>	<u>17,400</u>

#### Depreciation:

At 1 January 2006	1,235	-
Transfer from Property and equipment		903
Transfer from Prepaid lease rentals		332
Dn disposal	(1,235)	-
At 31 December 2006	<u>1,235</u>	<u>1,235</u>

#### Net book value:

At 31 December 2006	<u>-</u>	<u>16,165</u>
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## 17. OTHER ASSETS

	2006		2005	
	Group KShs'000	Company KShs'000	Group KShs'000	Company KShs'000
Staff debtors	34,334	34,328	36,655	36,644
Prepayments	23,431	13,432	18,010	18,010
Deposits and rent receivable	8,318	8,296	3,047	2,592
Other receivables	48,510	29,110	31,255	29,429
	<u>114,593</u>	<u>85,166</u>	<u>88,967</u>	<u>86,675</u>

Included in staff debtors is staff car loans of KShs 33,293,212 (2005 – KShs 33,320,058).

## 18. HOUSING DEVELOPMENT PROJECTS

	2006 KShs'000	2005 KShs'000
<b>Group:</b>		
<b>Housing projects</b>		
Komarock Housing Projects	<u>9,683</u>	<u>9,430</u>

Commitments in respect of these projects authorised but not paid as at 31 December 2006 amounted to Nil (2005 – Nil).

# NOTES TO THE FINANCIAL STATEMENTS (Continued)

## 37. FINANCIAL INSTRUMENTS (Continued)

### Interest rate risk

#### Contractual maturity analysis of assets and liabilities

The table below summarises the exposure to interest rate risks. Included in the table below are the group's assets and liabilities at carrying amounts, categorized by the earlier of contractual repricing or maturity dates:

	Average interest rate %	Due within 3 months KShs'000	Due between 3 and 12 months KShs'000	Due between 1 and 5 years KShs'000	Due after 5 years KShs'000	Non - interest bearing KShs'000	Total KShs'000
<b>Assets</b>							
Cash and bank balances	2.00%	179,455	-	-	-	-	179,455
Placements with other banks	6.36%	1,015,618	-	-	-	-	1,015,618
Investment in government securities	6.30%	347,735	79,019	470,000	-	-	896,754
Net mortgage advances to customers	6.63%	6,345,349	-	-	-	-	6,345,349
Other assets		-	-	-	-	114,593	114,593
Housing development projects		-	-	-	-	9,683	9,683
Property and equipment		-	-	-	-	337,269	337,269
Prepaid operating lease rentals		-	-	-	-	51,188	51,188
Intangible assets		-	-	-	-	49,299	49,299
Deferred tax		-	-	-	-	52,584	52,584
Taxation		-	-	-	-	30,072	30,072
Retirement benefit asset		-	-	-	-	51,967	51,967
<b>Total assets</b>		<b>7,888,157</b>	<b>79,019</b>	<b>470,000</b>	<b>-</b>	<b>696,655</b>	<b>9,133,831</b>
<b>Liabilities, shareholders' funds, loans and income notes</b>							
Customers' deposits	3.70%	3,022,863	3,422,185	1,119,071	54,604	-	7,618,723
Other liabilities		-	-	-	-	132,128	132,128
Deferred tax liability		-	-	-	-	10,217	10,217
Share capital		-	-	-	-	575,000	575,000
Reserves		-	-	-	-	747,013	747,013
Shareholders' income notes		-	-	-	-	50,750	50,750
<b>Total liabilities and equity</b>		<b>3,022,863</b>	<b>3,422,185</b>	<b>1,119,071</b>	<b>54,604</b>	<b>1,515,108</b>	<b>9,133,831</b>
<b>On balance sheet interest sensitivity gap</b>		<b>4,865,294</b>	<b>(3,343,166)</b>	<b>(649,071)</b>	<b>(54,604)</b>	<b>(818,453)</b>	<b>-</b>
<b>At 31 December 2005</b>							
Total assets		8,659,936	17,455	141,826	400,000	641,861	9,861,078
Total liabilities and equity		5,925,237	854,413	191,114	1,462,739	1,427,575	9,861,078
<b>On balance sheet interest sensitivity gap</b>		<b>2,734,699</b>	<b>(836,958)</b>	<b>(49,288)</b>	<b>(1,062,739)</b>	<b>(785,714)</b>	<b>-</b>

## 38. INCORPORATION

The company is incorporated as a limited company in Kenya under the Companies Act.

## 39. CURRENCY

These financial statements are expressed in Kenya Shillings

# HOUSING FINANCE PRODUCT NEWS

Our Mortgage interest rate have been reduced. The base rate now is 12.5%. The extension of the period to 20 years is geared towards making home ownership cheaper for all Kenyans. And we offer a Good Payers Discount of 0.5% off these rates.

So keep your repayment up to date and enjoy a lower rate of interest.

Plan	Period	Base	New Mortgage rate
Start-up Plan Mortgage	13-20 years	Base + 3.25%	15.75%
House Plan Mortgage	6-12 years	Base + 3.00%	15.50%
Ace Plan Mortgage	1-5 years	Base + 2.50%	15.00%

## Easycash ATM

With your Eash Cash Debit card, you can use it at any Housing Finance ATM, Ken-Switch branded ATM's and Pesa-Paint branded ATM's to withdraw your money at anyplace, anywhere and anytime. You can also use it to purchase goods at any merchant's outlets with a Senator and Ken switch Logo.



## INSURANCE DISCOUNT

We are happy to inform you that we have obtained a discount on the fire insurance policy premium, of 9.3% on the residential properties. The discount has been passed on to all mortgage customers effective 1 July 2006.

## ENHANCED MORTGAGE LIFE COVER

In recognition of the need to enhance your benefits under the group mortgage life cover, we have introduced an addition cover "Life plus " at a modest cost. The new cover has a lump sum benefit of Ksh. 500,000 or 1,000,000 payable to the dependents following the death of the borrower. It also has last expense of Ksh 100,000 payable within 48 hours of a borrower's death, to cater for funeral expenses. Kindly pick the consent form from your branch, fill in the information required and return it to us as soon as possible for you to be included in this cover.

## EQUITY RELEASE LOAN

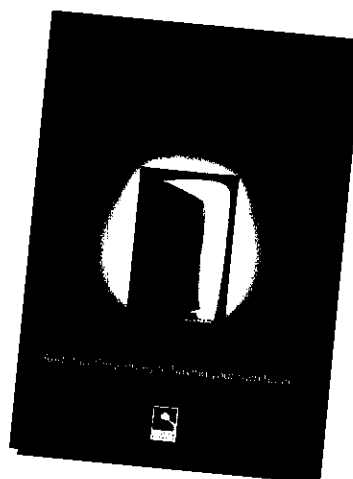
You can use your property title or lease to borrow money from us. Equity release loan allows you to turn either your land title or the repaid portion of

an ongoing loan into cash. The extension of the period to 20 years is geared towards making home ownership cheaper for all Kenyans. And we offer a Good Payers Discount of 0.5% off these rates.

So keep your repayment up to date and enjoy a lower rate of interest.

## JUHUDI ACCOUNT

With a minimum balance of Ksh. 500 you can operate a Juhudi account. The account has minimal charges and gives you the freedom to manage your funds at your convenience.



## MORTGAGE BROKERAGE

We have established Mortgage Brokerage Services with AAR Credit Services Ltd. You can now access our products through AAR Credit services. This comes with added benefits for AAR members.

## HOME OWNERSHIP SAVINGS PLAN

We have started a registered Home Ownership Savings Plan effective 1 January 2007 in accordance with the income tax act. Under the plan, a depositor is eligible to a deduction upto a maximum of Kes. 4,000.00 per month or Kes. 48,000.00 p.a in respect of funds deposited in the plan.

Further, interest earned on deposits not exceeding Kes. 3 million shall be exempted from tax.

## NOTES

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