2018 ANNUAL REPORT

AND FINANCIAL STATEMENTS

HF GROUP
Dreams Made Possible

HF Group Achieves Greatness at the CIO100 Gala Awards

HF Group won the **GOLD MARK** and **2018 PLUS ONE AWARD – FINANCIAL SERVICES SECTOR** at the **CIO100 Gala Awards.**

Our Chief Information Officer, George Njuguna, emerged East Africa's **CIO OF THE YEAR 2018**, in recognition of his exceptional contribution to the industry.

This is a great affirmation of our digital transformation journey that seeks to drive growth and business value through our digital banking platform **HF Whizz**.

These achievements could not have been possible without our customers and stakeholders.

Asanteni sana!

CONTENTS

DIRECTORS, OFFICERS AND ADMINISTRATION

DIRECTORS

Steve O. Mainda	Chairman
Robert Kibaara (Appointed on 1 March 2019)	Group Chief Executive Officer
Frank Ireri (Resigned on 31 January 2019)	Outgoing Group Managing Director
Benson I. Wairegi	
Peter K. Munga	
Adan D. Mohamed	
Constance Gakonyo	
Kaushik Manek	
Felister Kembi	
Gladys Karuri	

COMPANY SECRETARY

Regina Anyika
Rehani House
Kenyatta Avenue/Koinange Street
P.O. Box 30088
00100 Nairobi GPO

REGISTERED OFFICE

Plot No. LR 209/9054
Rehani House
Kenyatta Avenue/Koinange Street
P.O. Box 30088
00100 Nairobi GPO

SHARE REGISTRAR

Comprite Kenya Ltd.
2nd Floor, Crescent Business Centre
Parklands Road
P.O. Box 63428-00619
Nairobi

BANKERS

HFC Limited
Rehani House, Kenyatta Avenue
P.O. Box 30088
00100 Nairobi GPO

AUDITORS

KPMG Kenya
Certified Public Accountants
8th Floor, ABC Towers
Waiyaki Way
P.O. Box 40612
00100 Nairobi GPO

SUBSIDIARIES

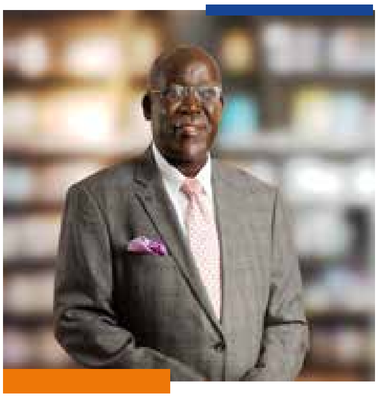
HFC Limited
HF Development and Investment Limited
First Permanent (East Africa) Limited
HF Insurance Agency Limited
HF Foundation Limited

PRINCIPAL LEGAL ADVISORS

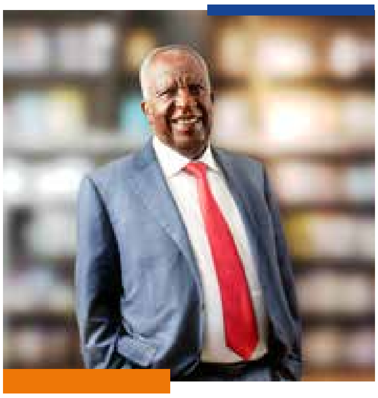
Walker Kontos Advocates
Hakika House
Bishops Road
P.O. Box 60680
00200 Nairobi City Square


GET INSTANT LOANS
DEPOSIT & TRANSFER CASH
BUY GOODS & PAY BILLS
SEND M-PESA
#BankSaveGrow
DOWNLOAD NOW
HF Whizz
10:30 AM
100%
VIEW ACCOUNT
ME
OUR SERVICES
BUY GOODS
SEND M-PESA
PAY BILL
TRANSFER CASH
MEAT
Dial *618#
Download on the App Store
ANDROID APP ON Google Play
HFGroupKE
HFGroupKE
Help line: 0800 721400

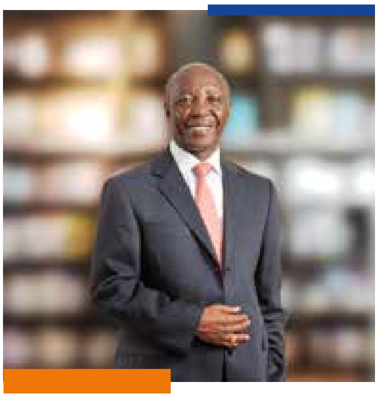
HF GROUP DIRECTORS



Steve Mainda, 73 years
GROUP BOARD CHAIRMAN



Peter Munga, 76 years
BOARD MEMBER



Benson Wairegi, 66 years
BOARD MEMBER

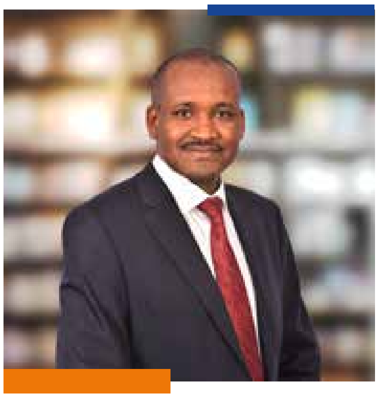
Adan Mohamed, 56 years
BOARD MEMBER

Constance Gakonyo, 54 years
BOARD MEMBER

Kaushik Manek, 62 years
BOARD MEMBER

Felister Kembi, 63 years
BOARD MEMBER

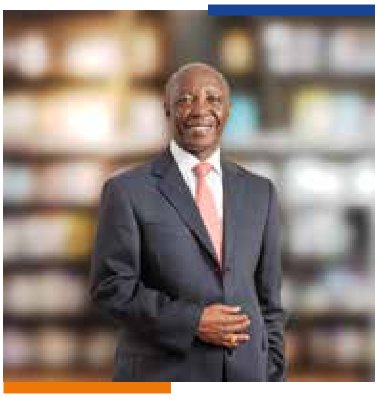
Gladys Karuri, 46 years
BOARD MEMBER



Robert Kibaara, 46 years
GROUP CHIEF EXECUTIVE OFFICER

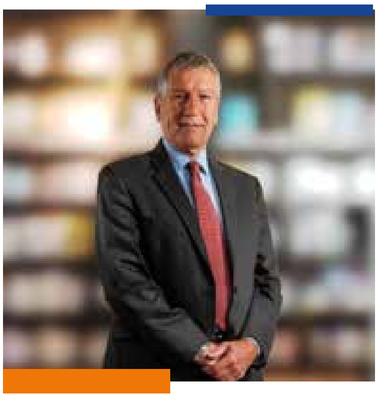
HFC DIRECTORS

Kaushik Manek, 62 years
HFC BOARD CHAIRMAN



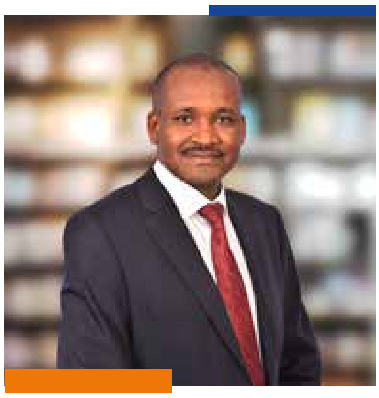
Benson Wairegi, 66 years
BOARD MEMBER

Gladys Ogallo, 53 years
BOARD MEMBER



Nicholas Ashford-Hodges, 69 years
BOARD MEMBER

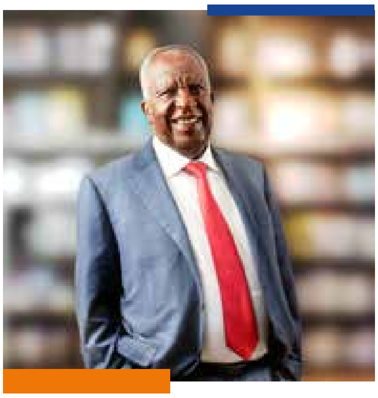
Shilpa Haria, 59 years
BOARD MEMBER



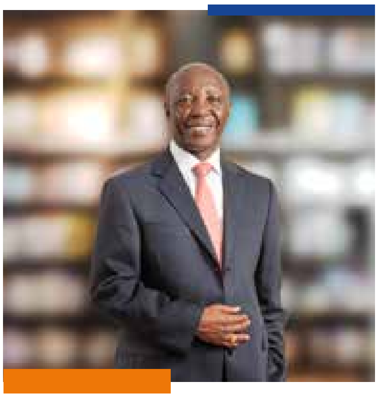
Robert Kibaara, 46 years
GROUP CHIEF EXECUTIVE OFFICER

HF DEVELOPMENT & INVESTMENT DIRECTORS

Adan Mohamed, 56 years
HFDI BOARD CHAIRMAN

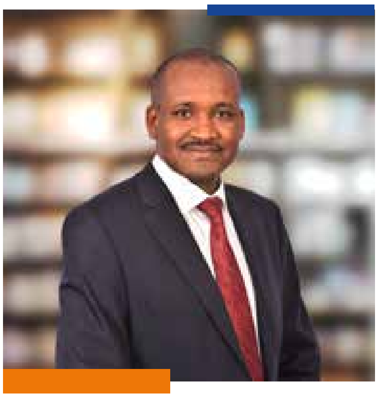


Peter Munga, 76 years
BOARD MEMBER



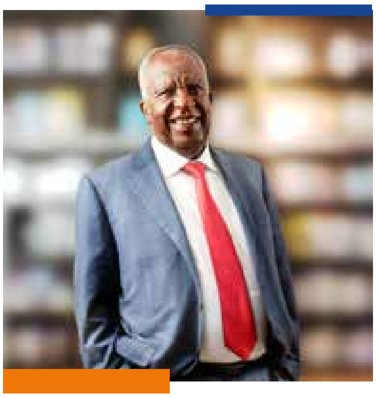
Benson Wairegi, 66 years
BOARD MEMBER

Caroline Ongeri, 51 years
BOARD MEMBER



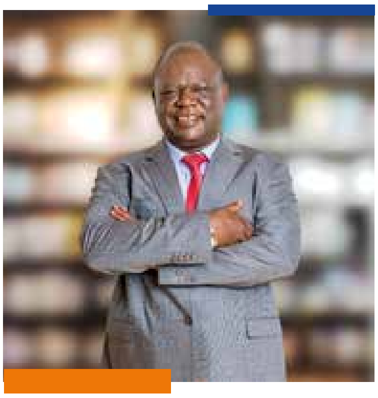
Robert Kibaara, 46 years
GROUP CHIEF EXECUTIVE OFFICER

HF FOUNDATION DIRECTORS



Peter Munga, 76 years
HFF BOARD CHAIRMAN

Ruth Kagia, 70 years
BOARD MEMBER (RETIRED)

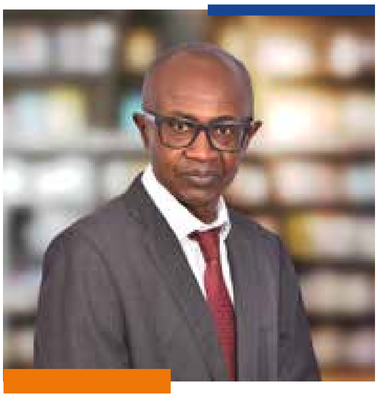


Christopher Khaemba, 59 years
BOARD MEMBER

Robert Kibaara, 46 years
HF GROUP CHIEF EXECUTIVE OFFICER

HF INSURANCE AGENCY DIRECTORS

Robert Kibaara, 46 years
HFIA BOARD CHAIRMAN



Patrick Mokaya, 51 years
DIRECTOR, BUSINESS DEVELOPMENT

Jane Surungai, 56 years
PRINCIPAL OFFICER & ASS. GENERAL MANAGER

BOARD OF DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2018

Dr. Steve Omenge Mainda, EBS - Chairman - Non Executive Director

Dr. Steve Mainda (EBS) is the current Chairman of HF Group PLC and was appointed director on 3rd December 2014. He has a broad and extensive background in finance, insurance, investment, education and management.

He is a Fellow of the Institute of Directors of London and an Associate Member of the Chartered Insurance Institute of London. He holds M.A and B.A Degrees from the Universities of Princeton and Cambridge. He sits on the Board of several companies in Eastern Africa viz: Continental Reinsurance, Shelter Afrique, Sasini Plc, Ryce East Africa, Dubai Islamic Bank Kenya among others.

Frank Ireri, EBS - Outgoing Group Managing Director

Mr. Frank Ireri, EBS was appointed Group Managing Director of HF Group PLC, a Non-Operating Holding Company approved by Central Bank of Kenya (CBK), effective 1st July 2015. Prior to his appointment, Frank Ireri was the Managing Director of Housing Finance Company Of Kenya Limited, a position he had held since July 2006, a total of nine years. He is a well-seasoned banker with more than 20 years standing experience and joined the Company from Barclays Bank of Kenya where he was Head of Operations for Barclaycard 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 an 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.

In 2011, he was awarded the Elder of the Burning Spear by former President Mwai Kibaki in recognition of his service to the nation in his various capacities. In 2014, he was declared the "Leadership & Ingenuity 2013 Kenya" winner in the Global 2014 Citi Distinguished Alumni Awards.

Frank holds a Bachelor of Commerce Degree from the University of Nairobi and is also a Certified Public Accountant (CPA K).

Robert Kibaara – Group Chief Executive Officer

Robert is a renowned banker, with over 24 years' experience and an excellent record of accomplishment in successfully driving change, revenue mobilization and delivering outstanding business results. He has previously held several leadership positions including Retail Director at NIC Bank; Executive Director - Retail and Business Banking at National Bank of Kenya; General Manager - Integrated Distribution for Southern Africa and General Manager Personal Banking & New Business at Standard Chartered Bank; among other executive positions at Barclays Bank of Kenya.

He holds a Bachelor's Degree in Banking and Finance from the University of Sunderland (UK) and a Post Graduate Diploma from the Chartered Institute of Marketing (CIM) UK.

Dr. Benson I. Wairegi, EBS - Non Executive Director

Dr. Benson I. Wairegi, EBS, has worked for Britam Holdings Plc in various capacities and is currently the Group Managing Director. He previously worked with Price Waterhouse, the forerunner of PricewaterhouseCoopers. He is a director at Britam Holdings Plc and the Chancellor of Kenyatta University. He is also the Chairman of Endeavor Kenya an organization headquartered in New York City that is pioneering the concept of high-impact entrepreneurship in growth markets around the world. He is a former Chairman of the Association of Kenya Insurers (AKI) and former Board member of the Board of Trustees of the Insurance Training and Education Trust (ITET).

Dr. Wairegi holds an Honorary Doctorate Degree (Honoris Causa) from Kenyatta University, Bachelor of Commerce and Master of Business Administration degrees from the University of Nairobi. He is a Certified Public Accountant (CPA-K). He has significant insurance and financial services industry experience.

BOARD OF DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

Dr. Peter K. Munga, EGH - Non Executive Director

Dr. Peter K. Munga, EGH is a Certified Public Secretary with vast experience in both public and private sector management. He holds two honorary doctorates, Doctor of Letters (Honoris Causa) from The University of Nairobi, and Entrepreneurship (Honoris Causa) from Kenya Methodist University. He has a diploma in Human Resources and Financial Management. He has received the highest presidential award to a civilian, the First Class Chief of the Order of the Burning Spear (CBS) and also the Second Class Order of the Golden Heart of Kenya (EGH) national decoration, for his outstanding contributions in economic development. Dr. Munga is the Chairman of Pioneer Group of Schools, Equatorial Nut Processors Ltd, Freshco Seeds Ltd and Murang'a Water and Sewerage Company (MWASCO). He is the current Chancellor of Pioneer International University. He is a Director with Britam Holdings Ltd and HF Group.

Adan D. Mohamed, Juris Doctor (JB), EBS - Non Executive Director

Mr. Mohamed joined the board on 15th October 2012. Adan has extensive knowledge and expertise in Law having engaged in legal representation in and outside the country. He has also engaged in the training and evaluation of law enforcement officials in matters involving access to justice and eradication of inequalities based on race, gender or national origin.

Constance Gakonyo, CPS (K), MCIArb, CBS - Non Executive Director

Ms. Gakonyo is a strategic management expert with extensive legal and corporate governance experience. She has held a variety of senior management positions including that of Legal Consultant and head of the performance management portfolio for SABMiller Africa Asia (Pty) Limited. She holds a Law Degree from the University of Nairobi and an MBA in Strategic Management. Constance is a member of the Law Society of Kenya (LSK), Certified Public Secretaries CPS (K) and the Chartered Institute of Arbitrators. She has sat on the Board of HF Group PLC (since 2014) and heads the Nomination and Governance Committee. Constance has also served on the Boards of East African Breweries Limited (EABL) and on the Group Boards of REAL Insurance Co. Ltd (Kenya, Malawi, Mozambique, and Tanzania).

Kaushik Manek, EBS - Non Executive Director

Dr. Kaushik Manek, EBS was appointed as a Non-Executive Director of HF Group PLC effective 26th June 2015. Upon completing his education, locally in Kenya and the UK, Dr. Manek joined the family business in 1978 and has since been instrumental in its growth from a small retail shop in Nairobi to multi-faceted business interests in Kenya.

Dr. Manek is committed to both social and community service. This is exhibited through his extensive involvement with Rotary since 1997, having worked through the ranks within the club level and eventually serving as District Governor in 2008- 2009. His social service spans beyond Rotary and is reflected through community leadership roles within the Lohana community and the Desai Memorial Foundation, amongst others.

Felister Kembi - Non Executive Director

Ms. Felister Kembi joined the board on September 2016. She is a graduate of the University of Nairobi with a degree in B.Com (Accounting). She is also a CPA (K) holder and a member of the Institute of Certified Public Accountants of Kenya (ICPAK). Felister has vast experience having worked for Kenya Airways, East African Portland Cement, Kenya Times, Bellhouse Mwangi, Ernst & Young and Roussel of EA later known as AgrEvo EA Ltd. mainly as an accountant, auditor and Finance Manager. She is also a director of Felicity Exclusive Designs, a major importer and distributor of clothing and household goods.

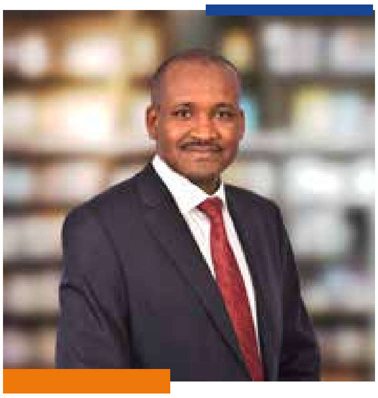
BOARD OF DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

Gladys Karuri - Non Executive Director

Gladys joined the HF Group board in 2016. She is currently the Group Finance & Strategy Director in Britam. A Certified Public Accountant (Kenya) CPA and a member of the Institute of Certified Accountants of Kenya, Gladys is a Mathematics and Economics graduate of the University of Nairobi and holds an MBA from the University of Warwick, Warwick Business School.

Gladys started her working career with PricewaterhouseCoopers working in both Kenya and the United Kingdom where she rose to the position of Senior Manager, Assurance. She left PricewaterhouseCoopers in 2007 and joined Britam as the Chief Finance Officer. In 2011 she was promoted to the position of Group Finance and Strategy Director of Britam Holdings Ltd. Gladys is also a Director of Continental Reinsurance Ltd.

SENIOR MANAGEMENT TEAM



Robert Kibaara, 46 years
GROUP CHIEF EXECUTIVE OFFICER

Jane Surungai, 56 years
PRINCIPAL OFFICER & ASS. GENERAL MANAGER

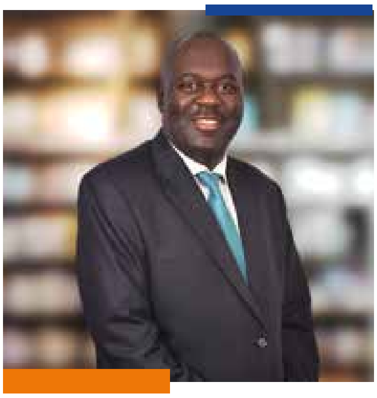
Peter Mugeni, 41 years
DIRECTOR, CREDIT

George Njuguna, 35 years
CHIEF INFORMATION OFFICER

Achieng Oluoch, 38 years
HEAD OF MARKETING

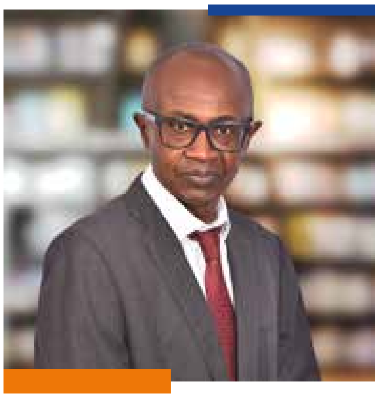
Edmund Muchemi, 39 years
AG. GROUP FINANCE DIRECTOR

SENIOR MANAGEMENT TEAM



Tom Shivo, 47 years
DIRECTOR, HUMAN RESOURCES

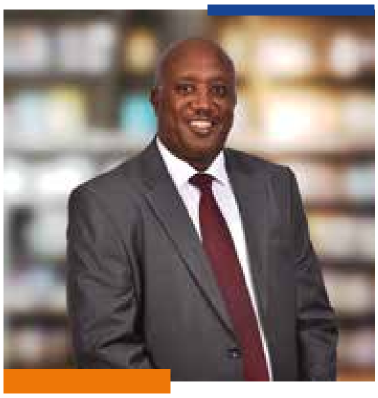
Regina Anyika, 51 years
DIRECTOR, LEGAL DIVISION & COMPANY SECRETARY



Patrick Mokaya, 51 years
DIRECTOR, BUSINESS DEVELOPMENT

Kennedy Gachoki, 43 years
HEAD OF RISK

Nancy Matimu, 44 years
CHIEF DIGITAL OFFICER



Joseph Ngare, 49 years
GENERAL MANAGER, AUDIT

Dorothy Jumba, 44 years
HEAD OF CUSTOMER SERVICE

SENIOR MANAGEMENT TEAM
FOR THE YEAR ENDED 31 DECEMBER 2018

Robert Kibaara – Group Chief Executive Officer

Robert is a renowned banker, with over 24 years experience and an excellent record of accomplishment in successfully driving change, revenue mobilization and delivering outstanding business results. He has previously held several leadership positions including Retail Director at NIC Bank; Executive Director - Retail and Business Banking at National Bank of Kenya; General Manager - Integrated Distribution for Southern Africa and General Manager Personal Banking & New Business at Standard Chartered Bank; among other executive positions at Barclays Bank of Kenya.

He holds a Bachelor's Degree in Banking and Finance from the University of Sunderland (UK) and a Post Graduate Diploma from the Chartered Institute of Marketing (CIM) UK.

Frank Ireri – Outgoing Group Managing Director

Frank was appointed Managing Director in July 2006, and Group Managing Director on 1st July 2015. He is a seasoned Banker with more than 20 years standing experience and joined the Company 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 the Philippines, Poland, Sri Lanka and Zambia.

In 2014, as part of the Citi Alumni Network, he was awarded the distinguished alumni award for Leadership & Ingenuity in recognition of his tremendous achievements and innovations in the Kenyan mortgage finance industry.

In 2011, the former President H.E. Mwai Kibaki conferred upon him the Elder in the second class of The Order of the Burning Spear (EBS) in recognition of his distinguished service rendered to the Nation. Frank holds a Bachelor of Commerce degree from the University of Nairobi and is a Certified Public Accountant (CPA K).

Sam Waweru – Outgoing Managing Director, HFC Limited

Sam joined HF Group in December 2005 as the Head of Internal Audit. He began his career at Ernst & Young in 1992 as an Accountant/ Auditor. He has also held the following positions prior to joining HFC; Senior Internal Auditor at Lonrho Africa Management Services, Head of Internal Audit at Uchumi supermarkets and Head of Internal Audit at Aga Khan Health Services, East Africa. Sam holds B.Com (Accounting) from the

University of Nairobi and a Certified Public Accountant of Kenya (CPA K).

Jane Surungai - Principal Officer & Assistant General Manager, HF Insurance Agency Limited (HFIA)

Jane joined the HF Group in November 2002 as Insurance Manager and has grown to the current position of AGM & Principal Officer, and is also a Director of HFIA. Jane has over 20 years' experience in insurance, having previously worked in the insurance industry. She holds a Bachelor of Commerce (Hons.) degree from the University of Nairobi, and is a Fellow of the Chartered Insurance Institute (UK) as well as Fellow of the Insurance Institute of Kenya.

Jane is an Executive member of the Insurance Institute of Kenya, the body that oversees professionalism in the insurance industry.

SENIOR MANAGEMENT TEAM
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

Peter Mugeni - Director, Credit

Peter is a seasoned banker, with over 15 years experience in Credit Risk Management and Operations, as well as leading large teams both regionally and across Africa. Through his experience, he has formulated and implemented business strategies which have made significant turnaround impact to the Organizations he has worked for. He joined HF Group from Standard Bank of South Africa where he was Credit Executive responsible for Sanctioning and Monitoring of Large Exposures from Stanbic Africa entities (including Kenya). Prior to that, he was the Head of Credit, Personal and Business Banking for Stanbic Bank Tanzania for 5 years.

Peter has previously worked at Housing Finance as an Accounts Officer, Credit Analyst and Assistant Credit Manager, and with Stanbic Bank Kenya Limited as Credit Origination Manager (Corporate & Investment Banking), Credit Evaluation Manager (Personal and Business Banking) and Head of Credit, Business Banking. He holds a Master of Science in Finance (Banking Option) and a Bachelor of Commerce degree (Finance Option) both from the University of Nairobi. In addition, he is a Certified Retail Banker (CRB), Certified Chartered Accountant (ACCA) and a Certified Bank Credit Evaluator.

Tom Shivo – Director, Human Resources

Tom is a seasoned HR practitioner with 24 years working experience, 20 of which have been in the Human Resources field. He has previously worked at Safaricom as the Head of Business Partners (Commercial Divisions); Airtel Africa as the HR Director (Talent Management) and had a stint in Nigeria as the HR Director for Airtel Nigeria. He has also worked at Kenya Airways, where he was the Head of HR Relationships & Reward, and also acted as the HR Director for close to a year. At Coca-Cola Sabco, he was the Country HR Manager for the Kenya business, and previous to this he was the HR Manager at The Nairobi Hospital. He has been a HR consultant with Hawkins Associates /KHI Training, and a teacher in his early career days.

Tom holds an MBA in Human Resources from University of Nairobi, a Bachelor of Education from Kenyatta University and a Higher National Diploma in Human Resources. He also holds an Advanced Leadership certificate from GIBBS Institute (Pretoria University) and Christ Church (Oxford University).

Regina Anyika – Director, Legal Division and Company Secretary

Regina joined HF Group PLC in September 2013. She is currently the Director – Legal Services and Company Secretary. Prior to joining the bank, Regina worked with the Co-operative Bank of Kenya Limited and Senator Cards Limited. She holds an MBA (Employee Relations) from the University of Leicester, LLB from the University of Nairobi, diploma from the Kenya School of Law and is a Certified Public Secretary of Kenya (CPS K) and an accredited Governance Auditor (CPS K).

George Njuguna – Chief Information Officer

George joined the company as the Chief Information Officer. He has over 15 years' experience in ICT. Specifically, he has over 10 years in banking related technology, transactional banking, product development, project management, digital channels, data security and system integration. He has held various technical and senior management roles locally, regionally and internationally. George holds a Bachelor of Science Degree and MBA from Geneva College in Pittsburgh Pennsylvania.

SENIOR MANAGEMENT TEAM
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

Achieng Oluoch - Head of Marketing

Achieng has over 13 years experience in marketing communications. Her current role as Head of Marketing includes spearheading the development and execution of marketing & communication strategies; management of the corporate brand image, market research and product development.

She holds a Master of Commerce Degree (IBM) from Strathmore University, Bachelor of Arts Degree in Communication and Media Technology (Public Relations), Maseno University and Diploma in Project Management from the Kenya Institute of Management.

Edmund Muchemi – Ag. Group Finance Director

Edmund joined the Company on 6 August 2007 as a Management Accountant for the Group and rose through the ranks to his current role as the Ag. Group Finance Director. Prior to joining the company, Edmund worked with the Equity Bank, Security Group Africa Ltd, and Muthaiga Golf Club. Edmund is a seasoned Accountant with over 17 years working experience in banking, security services and hospitality sector. He is a Qualified Accountant and a member of the Institute of Certified Public Accountants of Kenya (ICPAK).

Patrick Mokaya - Director, Business Development

Prior to joining HF Group Patrick worked in various capacities in corporate & commercial banking with Bank of Africa, Citibank, Credit Agricole Indosuez and Stanbic Bank. Patrick holds a BA Degree in Technology Management & Economics from Moi University and Global Executive MBA from USIU in association with Columbia Business School (USA). He is also an Associate of the Chartered Institute of Bankers (UK) and holds a Diploma in Bank Credit & Risk Management from Damelin School of Banking in South Africa.

Kennedy Gachoki - Head of Risk

Kennedy joined HF Group in November 2015 to oversee the Enterprise Risk Management Division with functional reporting responsibilities to the Board Risk Committee. He joined HF from Central Bank of Kenya (CBK) where he had served since June 2008 in Bank Supervision Department. He has vast experience in banking risk management processes including risk identification, risk measurement, risk control and risk monitoring. He has also participated in several international and local forums on banking risk management including compliance related trainings.

Kennedy holds a Masters Degree in Business Administration (MBA-Finance) from the University of Nairobi and a Bachelor of Commerce Degree in Accounting. He is also a Certified Public Accountant CPA (K).

Nancy Matimu - Chief Digital Officer

Nancy is a seasoned Commercial and Business Transformation practitioner with 18 years working experience cutting across technology and telecommunication sectors. She has previously worked at Safaricom as the Head of Consumer Products, Home and Content, Enterprise Products and Innovation; at Airtel Africa as the General Manager, Marketing, Products and Innovation Revenue. Before this, she worked at iWay Africa as the Head of Strategic Sales and Marketing; at Simba Group as the Corporate Solutions consultant, and at ICN Toshiba as the Group Sales and Marketing Manager for East Africa.

Nancy holds an MBA in Strategic Management from Strathmore University, a Bachelor of Environmental Studies from Kenyatta University and a CIM Post Graduate Diploma in Marketing. She also holds Advanced Leadership certificates from Strathmore University in Advanced Management Program (AMP) and Chief Executive Program (CEP); Global Leadership program from INSEAD Business School Abu Dhabi campus among others.

SENIOR MANAGEMENT TEAM
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

Dorothy Jumba - Head of Customer Service

Dorothy is currently the Head of Customer Service at HF Group. She is a Customer Experience professional with 12 years experience in Customer Experience industry having served in various capacities including Call Centre management. Prior to joining the company, she was an Operations Manager at the Safaricom Contact Centre.

Dorothy holds an MBA Degree in Strategic Management from University of Nairobi, a BSc. Degree in Horticulture from Egerton University and PRINCE2 Practitioner certification.

Joseph Ngare - General Manager, Audit

Joseph joined HF Group on 19th April, 2010 as the Head of Audit. Prior to joining the company, Joseph worked with Gulf African Bank and Cooperative Bank of Kenya Limited.

Joseph holds a Bachelor of Commerce Degree (Finance Option) and is a qualified Certified Public Accountant (Kenya), Certified Internal Auditor (CIA) and a Certified Quality Assessor (QA).

NOTICE OF ANNUAL GENERAL MEETING

To the Shareholders of HF GROUP Plc

NOTICE IS HEREBY GIVEN that the 53rd Annual General Meeting of the Company will be held at Nairobi on Friday 26th April 2019 at Kenyatta International Convention Centre (KICC) AMPHITHEATRE at 11.00 am to conduct the following business:

1. To table the proxies and note the presence of a quorum.
2. To read the notice convening the meeting.
3. To receive and, if approved, adopt the audited Balance Sheet and Accounts for the year ended 31st December 2018, together with the Chairman's, the Directors' and Auditor's Reports thereon.

4. To note that the Directors do not recommend the payment of a dividend for the financial year ended 31st December 2018.

5 To elect Directors:
   a) Mr. Adan Mohammed retires by rotation in accordance with Article 105 of the Company's Articles of Association and, being eligible, offers himself for re-election.
   b) Dr. Steve Omenge Mainda retires by rotation in accordance with Article 105 of the Company's Articles of Association, and having attained the age of seventy years further retires in accordance with the Code of Corporate Governance Practices for Issuers of Securities to the Public 2015 and being eligible, offers himself for re-election.
   c) Dr. Peter Kahara Munga retires by rotation in accordance with Article 105 of the Company's Articles of Association, and having attained the age of seventy years further retires in accordance with the Code of Corporate Governance Practices for Issuers of Securities to the Public 2015 and being eligible, offers himself for re-election.

6. In accordance with the provisions of Section 769 of the Companies Act, 2015 the following Directors, being members of the Group Board Audit & Risk Committee be elected to continue to serve as members of the said Committee:-
   - Ms. Felister Kembi
   - Mr. Adan Mohamed
   - Ms. Gladys Karuri

7. To approve the Directors Remuneration.

8. To note that the auditors, KPMG Kenya, will continue in office in accordance with Section 721 (2) and 724 of the Companies Act, No. 17 of 2015 and to authorize the Directors to fix their remuneration.

SPECIAL BUSINESS

9. To consider and, if thought fit, to pass the following resolution as an Ordinary Resolution:
   "THAT the nominal share capital of the Company be increased from Kshs. 2,500,000,000 to Kshs 5,000,000,000 by the creation of an additional 500,000,000 new ordinary shares of Kshs.5 each to rank pari passu in all respects with the existing ordinary shares of the Company"

BY ORDER OF THE BOARD
Regina Anyika
Company Secretary
P.O. Box 30088, GPO 00100
NAIROBI
Date: 3rd April 2019

NOTICE OF ANNUAL GENERAL MEETING

To the Shareholders of HF GROUP Plc (Continued)

NB:

1. A member entitled to attend and vote at the above meeting is entitled to appoint a proxy to attend and vote on his behalf. A proxy need not be a member. A form of proxy may be obtained as indicated in note 2 below and should be returned to The Registrar, HF Group Plc, Rehani House, Kenyatta Avenue, P.O. Box 30088, GPO 00100, Nairobi, or to the Shares Registrar Comprite Kenya , Crescent Business Centre, 2nd Floor, Opposite MP Shah Hospital to arrive not later than 11 AM on 24th April 2019.

   If the appointer is a corporation or Government office, the instrument appointing the proxy shall be given under its common seal or under the hand of an officer or duly authorized attorney of such corporation or Government office.

2. A copy of this notice, the proxy, the entire Annual Report & Accounts may be viewed on the Company's website at www.hfgroup.co.ke or a printed copy may be obtained from the Registered Office of the Company, Rehani House, Kenyatta Avenue/Koinange Street, P.O. Box 30088-00100 GPO, and Nairobi and from all our registered Branches countrywide.

NOTISI KUHUSU MKUTANO MKUU WA PAMOJA WA MWAKA

Kwa Wanahisa wa HF GROUP Plc

NOTISI INATOLEWA HAPA KWAMBA, mkutano wa 53 wa pamoja wa mwaka wa kampuni utafanyika jijini Nairobi Ijumaa Aprili 26, 2019 katika Kenyatta International Convention Centre (KICC) AMPHITHEATRE kuanzia saa tano asubuhi ili kuangazia maswala yafuatayo ya kibiashara;

1. Kuangazia mawakala na kutambua akida iliyoko.
2. Kusoma Notisi ya kuitishwa kwa mkutano.
3. Kupokea na endapo itaonekana kuwa sawa,kupitisha mizania na hesabu kwa kipindi cha mwaka uliomalizika Desemba 31, 2018 pamoja na ripoti ya Mwenyekiti, Wakurugenzi na Wakaguzi wa pesa.
4 Kutambua kwamba wakurugenzi hawatoi pendekezo la mgawo wowote wa faida kwa kipindi cha mwaka uliomalizika Desemba 31, 2018.
5 Kuwachagua wakurugenzi;
   a) Bw. Adan Mohammed anastaafu kwa zamu kwa mujibu wa kifungu nambari 105 cha sheria za makampuni na kwa kuwa anastahili, amejitokeza ili kuchaguliwa tena.
   b) Dkt. Steve Omenge Mainda anastaafu kwa zamu kwa mujibu wa kifungu nambari 105 cha sheria za makampuni na kwa kuwa ametimiza umri wa miaka 70 anastaafu kwa mujibu wa taratibu za maadili ya usimamizi wa mashirika ya utoaji wa hisa kwa umma. Kwa kuwa anastahili, amejitokeza ili kuchaguliwa tena.
   c) Dkt. Peter Kahara Munga anastaafu kwa zamu kwa mujibu wa kifungu nambari 105 cha sheria za makampuni na kwa kuwa ametimiza umri wa miaka 70 anastaafu kwa mujibu wa taratibu za maadili ya usimamizi wa mashirika ya utoaji wa hisa kwa umma. Kwa kuwa anastahili amejitokeza ili kuchaguliwa tena.
6. Kwa Mujibu wa sehemu ya 769 ya sheria za makampuni ya mwaka 2015, wakurugenzi wafuatao ambao ni wanachama wa kamati ya kundi kuhusu uhasibu na athari ichaguliwe ili iendelee mbele na jukumu la kuhudumu kama wanachama wa kamati iliyotajwa.

   - Ms. Felister Kembi
   - Mr. Adan Mohamed
   - Ms. Gladys Karuri

7. Kupitisha marupurupu ya wakurugenzi.
8. Kutambua kwamba wakaguzi wa pesa KPMG Kenya, wataendelea mbele na jukumu lao kwa mujibu wa sehemu ya 721 (2) na 724 ya sheria za makampuni nambari, 17 ya mwaka 2015 na kuwapa wakurugenzi uhuru kuamua marupurupu yao.

SHUGHULI MAALUM

9. Kuzingatia na endapo itaonekana kuwa sawa kupitisha azimio lifuatalo kama azimio la kawaida;
   "KWAMBA, kiwango cha juu cha mtaji wa hisa za kampuni kiongezwe kutoka Kshs.5,000,000,000 kwa kubuni hisa mpya za ziada za kawaida 500,000,000 kwa Kshs.5 kila moja ili kuwa sawa kwa hali yoyote na hisa zilizoko za kawaida za Kampuni."

KWA AMRI YA HALMASHAURI
Regina Anyika
Katibu wa Kampuni
SLP 30088, GPO 00100
NAIROBI
Imunukuliwa Aprili 3, 2019

NOTISI KUHUSU MKUTANO MKUU WA PAMOJA WA MWAKA

Kwa Wanahisa wa HF GROUP Plc

Muhimu:

1. Mwanachama aliyetimiza masharti ya kuhudhuria na kupiga kura wakati wa mkutano uliotajwa hapo juu anaweza kumteua wakala kuhudhuria na kupiga kura kwa niaba yake. Si lazima kwa wakala huyo kuwa mwanachama. Fomu ya uwakala imeambatanishwa hapa na inaweza kurejeshwa kwa Registrar, HF Group PLC, Rehani House, Kenyatta Avenue Slp 30088 GPO 00100 Nairobi na kupokelewa kabla ya saa Tano Asubuhi Aprili 24, 2019.

   Endapo wakala aliyeteuliwa ni shirika au ofisi ya serikali, stakabadhi iliyomteua iwe imepigwa mhuri na kutiwa sahihi na Afisa aliyeidhinishwa na shirika au ofisi ya Serikali.

2. Nakala ya notisi hii, wakala, ripoti kamili ya mwaka na hesabu za pesa zinaweza kupatikana kupitia wavuti wa kampuni www.hfgroup.co.ke au nakala iliyochapishwa inaweza pia kupatikana kupitia ofisi za kampuni zilizosajiliwa katika jumba la Rehani House, Kenyatta Avenue/ Koinange Street, Slp 30088-00100 GPO na Nairobi na pia kupitia matawi yetu yaliyosajiliwa kote nchini.

GROUP OVERVIEW

HF Group Plc, was registered as a non–operating holding company (under the Banking Act Cap.488), regulated by the Central Bank of Kenya (CBK) in August 2015. The non–operating holding company was set up to enhance corporate governance, provide oversight in management of the subsidiaries and ensure optimal growth at both Group and subsidiary levels.

The Group is listed on the Nairobi Securities Exchange (NSE), and has four operational subsidiaries;

- HFC Limited – licensed to carry out the business of mortgage finance as well as banking services under the Banking Act.
- HF Development and Investment Limited – (formerly known as Kenya Building Society Limited) undertakes real estate development.
- HF Insurance Agency Limited – Bancassurance solutions
- HF Foundation Limited - The Group's social investment arm

The Group is a provider of multidimensional financial services that power the potential of its customers.
These services include;

- Corporate & Institutional banking
- SME banking
- Retail banking
- Digital banking
- Property finance & development
- Bancassurance

OUR GROUP HISTORY

INCORPORATION 1965–1989

THE COMPANY WAS INCORPORATED IN 1965

- Founding investors being CDC (60%) and GoK (40%)
- GoK and CDC become equal shareholders in 1970
- From "In Pursuit of Shelter" to "The Rock of Kenya"
- 4 Branches

PUBLIC LISTING 1992–2000

LISTED ON THE NSE IN 1992

- CDC and GoK shareholding of 30.4% each and Kenyan investors 39.2%
- Upgrade banking system to Bank Plus
- In 1989, GoK reduced the shareholding to 7.3% and Kenyan investors to 62.3%
- First website launched

POSITIONING 2000–2010

FROM HFCK TO HOUSING FINANCE

- Rebranding to Housing Finance in 2002
- From the "Rock of Kenya" to "Turning Dreams Into Homes"
- Implemented Equinox Core Banking System
- Sale of CDC shares in 2007 to Britam and Equity Bank
- Rights Issue in 2008
- MTN issued in 2010 for KShs. 7B

DIVERSIFICATION 2011–2016

INCORPORATION OF HF GROUP

- MTN issued in 2012 for KShs. 3B
- In 2014, Britam increases shareholding
- Rights Issue in 2015
- Rebranding from Housing Finance to HF Group with 4 subsidiaries
- Launch full service banking proposition under Vision 2020
- From "Turning Dreams Into Homes" to "Dreams Made Possible"
- Implemented new core banking system

TRANSITION 2017

FULL SERVICE BANKING

- Repayment of KShs. 7B bond
- Launch - MasterCard, Internet Banking and Digital Website

DIGITAL TRANSFORMATION 2018

- Launch of HF Whizz digital banking platform
- Completion of Komarock Heights Phase 1
- Recognition of HF Whizz as an innovative digital banking platform – 2018 CIO East Africa Awards,Gold Mark and Plus One Award - Best Financial Services Sector Awards

GROUP OVERVIEW

Mission and Vision

Our Mission

Where we are going

To be the leading provider of integrated solutions for the acquisition, development and improvement of property in Kenya.

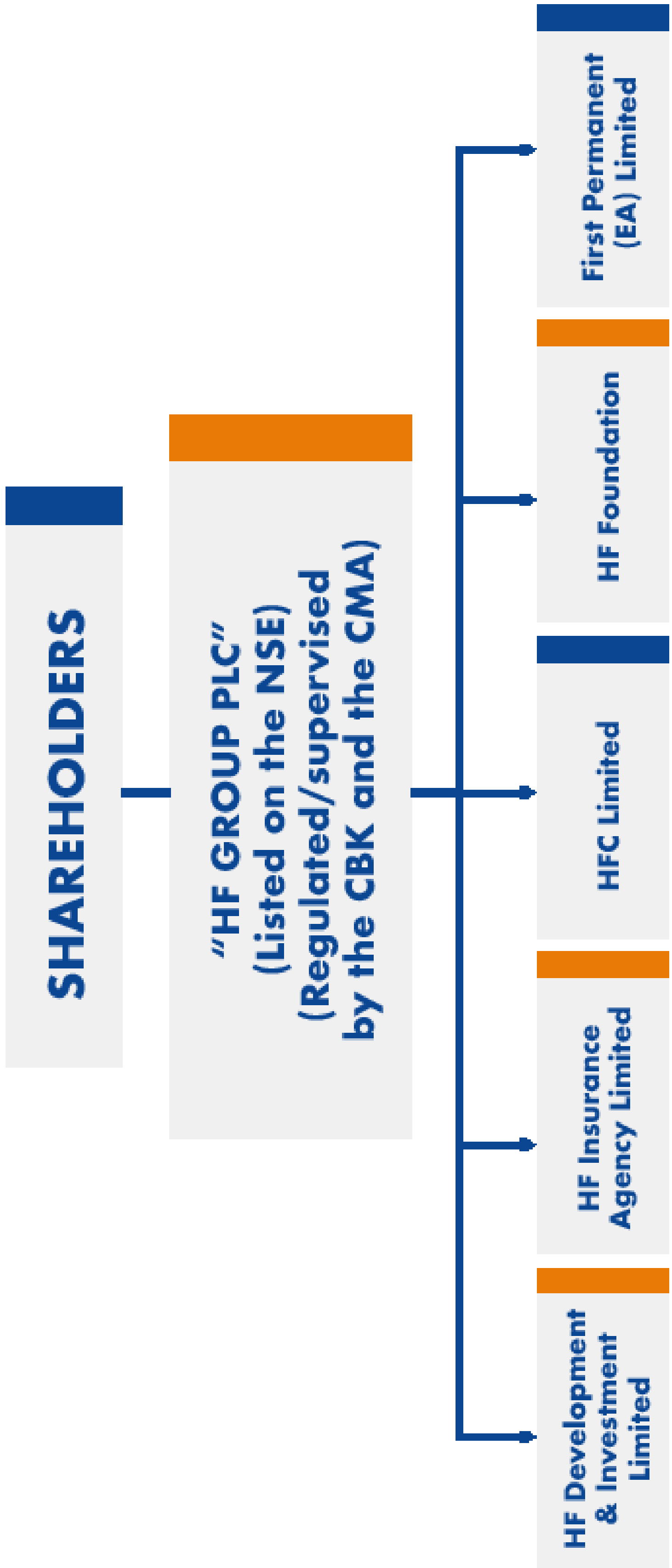
Our Vision

Our non-negotiable commitments

We will be the leading **integrated solutions enabler** for the property industry. We will offer innovative products and services, delivered under one roof by exceptionally committed people to enhance shareholder value. We will operate across the property value-chain as suppliers and financiers that offer unique solutions to all while being environmentally responsible.

GROUP OVERVIEW

The Group Structure



GROUP OVERVIEW

GROUP OVERVIEW

BUSINESS TRANSFORMATION STRATEGY

The Group has embarked on an aggressive business transformation strategy to turn around performance and accelerate growth to profitability by end of 2019. This is anchored on three structural service areas – building a digital bank, expansion into new banking segments and maintaining dominance in mortgage finance.

Building a digital bank

HF Group is taking advantage of emerging opportunities in the market to build a digital bank through its digital financial services unit. The Group's digital innovation is customer led, with products and services geared towards providing an end-to-end digital experience that allows customers to self-serve from wherever they are on the globe. In July 2018, the business launched its digital banking platform, HF Whizz, which has created efficiency in service delivery and improved customer experience. Through HF Whizz the business has become accessible to new customer segments that would otherwise be difficult to reach with the brick and mortar model.

The digital banking business has already broken even and is set to contribute to growth in business performance. Since its launch, HF has acquired over 550,000 new customers, reflecting a 600% jump in customer numbers; disbursements of over 1,000 loans per day with the number of disbursements growing daily and registered transactions exceeding Kshs.2.5 billion.

HF's business operating model is now anchored on DevOps and Agile framework that brings together technology, change and product development under one umbrella for faster releases and response to customer feedback on service improvement. The Group continues to invest in the right people with requisite technology expertise including big data, analytics and Artificial Intelligence to ensure delivery on responsive and data led innovation.

The digital transformation strategy is already receiving recognition in the industry. At the 2018 CIO East Africa Awards, HF won the Gold Mark Plus One Award - Best Financial Services Sector, for its innovative digital banking platform, HF Whizz. During the same awards, the Group CIO, George Njuguna was named the CIO of the year 2018.

The Group also received runners up award for Best Emerging Bank App at the 2018 Digital Inclusion Awards.

Expansion into new banking segments

As part of the full banking service transformation, the business has diversified into new segments; diaspora banking, SME banking, institutional banking and personal banking. This expansion is informed by the need to reduce the concentration in real estate, which is capital intensive and requires long term funding. With these new segments, the business is able to lower the cost of funding whilst serving customers' holistic banking needs.

Maintaining dominance in mortgage finance

In 2018, the Group completed and handed over to buyers the first phase of Komarock Heights consisting of 480 apartments. The Group also completed the development of 248 apartments at Richland Pointe along Kamiti Road, which culminated in an official launch ceremony in partnership with Shelter Afrique, who financed the project to the tune of KShs. 700million.

Moving forward, the business will concentrate its efforts on mortgage financing to end buyers. HF is one of the few players that have invested in the Kenya Mortgage Refinance Company (KMRC), which is set to unlock funds for lending to developers and buyers. This is poised to accelerate affordability of housing in line with the Housing Pillar of the Government's Big Four Agenda.

GROUP OVERVIEW
BUSINESS TRANSFORMATION STRATEGY (CONTINUED)

Non-Performing Loans (NPL) Management and Credit Quality Control

In addition to the three structural service areas, HF Group has put in place strategies to improve the quality of the lending book i.e. non-performing loans management and credit control. HF Group's non-performing loans are predominantly as a result of developers it has financed being unable to service their facilities, due to inability to realise projected sales revenue, resulting from the slowdown in the real estate sector. As such, the NPL Management Strategy entails working with these developers on joint marketing initiatives to increase visibility and take rate for their properties. One such initiative is the recently launched property sales campaign dubbed "Shika Nyumba na HF" offering 100 percent financing and reduced prices by up to 30%.

In addition, the business is offering a number of restructuring packages to distressed borrowers, including but not limited to;

Private Treaty Sales and Negotiated Settlements. HF Group will also be offering Business Solutions to those corporate entities experiencing cash flow challenges. These solutions include a restructure of the business entities, stand-still options, and other loan extension remedies to address short-term challenges.

CHAIRMAN'S STATEMENT

Steve Omenge Mainda, **EBS**
Chairman

Dear Shareholders,

On behalf of the Board of Directors of HF Group PLC, I welcome you to the 53rd Annual General Meeting of HF Group. It is also my pleasure to present to you the performance for the period ending 31 December 2018. The report also highlights economic, environmental, regulatory issues, opportunities and challenges, that influenced the business performance during the year and the strategic initiatives that HF Group is undertaking to steer business growth.

Economic overview

The global economy was reasonably upbeat. The year saw an improvement in general Kenyan economic performance, with an estimated GDP growth of 5.9% compared to 4.9% in 2017, attributed to favourable weather conditions and political stability. However, the public debt–to-GDP ratio increased considerably over the past five years to 57% at the end of June 2018, driven by infrastructural projects as well as the need to bridge the tax revenue deficit.

During 2018, the Central Bank of Kenya reduced the Central Bank Rate (CBR) twice to the current 9%. This slowed down the private sector credit growth especially among small and medium enterprises. Additionally the real estate sector had a bearish run during the year. A July/September report by the Kenya National Bureau of Statistics indicates that the property sector posted a growth of 5.8 per cent – its slowest rate since the 5.4 per cent recorded in the last quarter of 2014. This subdued demand for property due to the credit crunch, has affected many developers' ability to repay their bank loans.

These challenges, coupled with HF Group's over reliance on property development and finance, adversely affected business performance during the year. Our responsibility is to carry out business in a way which not only provides returns for our shareholders but also delivers value to society. We have also committed to achieving our goals and being accountable to our stakeholders.

CHAIRMAN'S STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

Turning around the business and the year ahead

As a Board, we appreciate the prevailing dynamics and the fact that we must conduct our business differently in order to remain afloat and flourish. The business has experienced headwinds but the Group is determined to turnaround the business and reclaim our previous record of delivering value for all our stakeholders. As such, the Group has instituted a two-year strategy to turn around the business back to profitability. This strategy focuses on diversification of HF business portfolio, whilst ring fencing our property business. Further, the business is investing in an omni-channel banking experience that is set to deliver operational excellence and best in class customer experience. Our aim is to establish a full service banking capability espousing a digital first, customer first operating model. HF Group will keep a watchful eye on the business and seize the opportunities as and when they arise, embracing technological advancement and innovation, and continuing to develop attractive value propositions for our customers. The Board will also focus on sustaining resilience by enhancing our brand image and viable performance.

Change of guard

In December 2018, the Board appointed Mr. Robert Kibaara, as the new Group Chief Executive Officer. I am proud to introduce to you to Mr. Kibaara, a seasoned career banker and business executive with an excellent record of success in driving change, revenue mobilization and delivering outstanding business results. He brings to the Group new dynamic leadership and agility to steer the business in the right direction. The Board also takes this opportunity to appreciate the former Group Managing Director, Mr. Frank Ireri, who served the Group for the last 13 years.

Brand Recognition

Despite challenges in performance, HF Group made great strides with the digital transformation strategy that saw the Group recognized as an industry leader in digital banking. The work on HF digital financial services platform dubbed HF Whizz won a number of accolades, of note being the Gold Mark award in recognition for excellence in Enterprise Information Technology Adoption during the 2018 CIO East Africa's Awards. HF Group congratulates Mr. George Njuguna, the Group Chief Information Officer, who was declared 2018 CIO of the Year during the same awards.

The Group has made efforts to ensure that the customer remains at the centre of operations, and will continue to invest in digital technology to improve efficiencies, customer experience and deliver on the bottom line.

Sustainability

The Group has adapted Sustainability Reporting and the maiden report is now available. This report marks a journey to highlight the sustainable business practices that HF Group has undertaken over the years and which the Group is deliberately pursuing for the betterment of business and the environment.

Conclusion

On behalf of the Board, I extend sincere gratitude to our shareholders, customers and partners for the unwavering support and contribution they have made in 2018. Equally, I thank the employees for their commitment, investors for their unrelenting confidence in HF Group, and our regulators for their prudential guidance. I would also like to express gratitude to my colleagues on the Board for their constant guidance and responsiveness in addressing challenges we have faced over the years.

The Board has put in place measures for regular and proactive review of our strategic initiatives, to ensure that the business performance is moving in the right trajectory. Our commitment to you as a Board is that we will sail through these headwinds and deliver a formidable business. We will equally keep our eyes open to find new business solutions to catalyze further growth opportunities in the long run.

Steve O. Mainda, EBS
Board Chairman

Date: 28 March 2019

TAARIFA KUTOKA KWA MWENYEKITI
KWA KIPINDI CHA MWAKA ULIOMALIZIKA DESEMBA 31, 2018

Kwa wanahisa,

Kwa niaba ya Halmashauri ya Wakurugenzi wa HF Group PLC, ningependa kuwakaribisha kwenye Mkutano wa 53 wa pamoja wa mwaka wa HF Group. Pia, ni fahari kwangu kuwaletea matokeo ya kipindi cha mwaka uliomalizika Desemba 31, 2018. Pia, ripoti hii itaangazia mazingira ya kiuchumi, maswala ya udhibiti, nafasi na changamoto ambazo ziliathiri matokeo ya biashara wakati wa kipindi hiki cha mwaka pamoja na mikakati ambayo HF Group inatekeleza ili kuendeleza ukuaji wa biashara.

Mtazamo wa Kiuchumi

Kwa kiasi, uchumi wa dunia ulikuwa ni wa kutia moyo. Kipindi hiki cha Mwaka, kilishuhudia ustawi wa jumla wa matokeo ya kifedha nchini Kenya kwa kadirio la asilimia 5.9 (5.9%) ikilinganishwa na asilimia 4.9 (4.9%) mwaka 2017. Ukuaji huu ulichangiwa pakubwa na hali nzuri ya anga na pia uthabiti wa kisiasa. Hata hivyo, deni la kitaifa ikilinganishwa na kiwango cha ukuaji wa kiuchumi liliongezeka mno kipindi cha miaka 5 iliyopita hadi asilimia 57 (57%) kufikia Juni 2018 kutokana na maendeleo ya miundo misingi pamoja na hitajiko la kuziba mwanya wa pengo la mapato yanayotokana na ushuru.

Wakati wa kipindi cha mwaka 2018, benki kuu ya Kenya ilipunguza kiwango cha riba (CBR) mara mbili hadi kile cha sasa cha asilimia 9 (9%). Hali hii ilipelekea kushuka kwa ukuaji wa mikopo katika sekta za kibinafsi hasa miongoni mwa chumi ndogo na zile za kadri. Zaidi ya hayo, sekta ya ujenzi wa mitaa ilikumbwa na misuko suko wakati wa kipindi hiki cha mwaka. Ripoti ya mwezi Julai/ Septemba iliyotolewa na taasisi ya utafiti ya kitaifa nchini Kenya inaonyesha kwamba, sekta ya mali ilisajili ukuaji wa asilimia 5.8 (5.8%) ambacho ni kiwango cha chini sana tangu iandikishe asilimia 5.4 (5.4%) kipindi cha mwisho mwaka 2014. Kushuka huku kwa mahitaji ya mali kulitokana na kushuka haraka kwa mikopo na kumeathiri pakubwa uwezo wa wastawishaji wengi wa mali kulipia mikopo yao ya benki.

Changamoto hizi pamoja na kuendelea kwa HF Group kutegemea ustawishaji wa mali na fedha, kuliathiri pakubwa matokeo ya fedha wakati wa kipindi hiki cha mwaka. Wajibu wetu ni kutekeleza shughuli za biashara kwa njia ambayo, bali na kuleta mapato kwa wanahisa wetu, pia italeta thamani kwa shirika. Pia, tumejitolea kuafikia malengo yetu ya kuwajibikia washika dau wetu.

Mabadiliko ya Biashara na Mwaka Ulio Mbele

Kama halmashauri, tunatambua mabadiliko yaliyoko sasa na hali kwamba lazima tutekeleze biashara zetu kwa njia tofauti ili kutuwezesha kusalia imara na kunawiri. Biashara imekabiliwa na mwimbi lakini kundi lina imani kubadilisha hali yake na kutwaa tena rekodi yetu ya zamani ya kuzalisha thamani kwa wadau wetu. Kwa sababu hiyo, kundi limezindua mkakati wa miaka mbili kuirejesha biashara kuzalisha faida. Mkakati huu unalenga upanuzi wa biashara zake huku likilinda raslmali zake. Zaidi ya hayo, biashara inawekeza kwenye mfumo wa matumizi ya mitandao ambao unatarajiwa kufanikisha utoaji huduma kwa wateja. Lengo letu ni kutambua huduma kamili na za haraka za benki kwa wateja kupitia matumizi ya dijiteli.

Kundi la HF litakuwa macho kwenye biashara na kutwaa nafasi zinazojitokeza, kuzingatia matumizi ya teknolojia, ubunifu na kuzidi kubuni mipango yenye thamani kwa wateja wetu. Halmashauri itaangazia udumishaji wa kukabiliana na athari kwa kuimarisha uwepo wa bidhaa zetu na kuzalisha matokeo.

Mabadiliko Kwenye Uongozi

Mnamo Desemba 2018, Halmashauri ilimteua Bw. Robert Kibaara kuwa Afisa Mkuu Mtendaji. Nina furaha kumjulisha kwenu Bw. Robert Kibaara Mwenye tajriba ya muda mrefu kuhusu maswala ya benki na Afisa Mkuu wa biashara aliye na rekodi ya ufanisi wa kuleta mabadiliko, kuhamasisha mapato na kuleta matokeo ya kufana. Ameliletea kundi maongozi mapya na uwezo wa kuendesha biashara katika mwelekeo unaofaa. Pia, halmashauri inachukua nafasi hii kutoa shukrani kwa Afisa Mkuu Mtendaji wa zamani Bw. Frank Ireri ambaye alilihudumia kundi kwa muda wa miaka kumi na tatu.

TAARIFA KUTOKA KWA MWENYEKITI

KWA KIPINDI CHA MWAKA ULIOMALIZIKA DESEMBA 31, 2018

Kutambuliwa kwa Bidhaa

Licha ya changamoto za matokeo, HF ilipata mafanikio huku agenda ya mabadiliko ya kidijiteli yakilifanya kundi kutambuliwa kama kiongozi wa benki kwenye matumizi ya mfumo huu kwenye biashara. Kazi katika HF kwenye mfumo wa utoaji huduma kupitia dijiteli uliopewa jina HF Whizz ulishinda matuzo kadhaa hasa tuzo la Gold Mark lililotambuliwa kwa ufanisi wa uwekezaji kwenye matumizi ya teknolojia ya habari na mawasiliano katika kipindi cha mwaka 2018 kwenye CIO East Africa Awards. HF inatoa heko zake kwa Bw. George Njuguna Afisa Mkuu wa mawasiliano aliyetangazwa kuwa mshindi wa CIO wa mwaka wakati wa hafla hiyo ya utoaji matuzo.

Kundi limefanya juhudi kuhakikisha kwamba mteja anasalia kuwa kitengo cha kati cha shughuli zake na litaendelea kuwekeza kwenye mfumo wa teknolojia ya kidijiteli ili kuimarisha utoaji huduma, hisia za mteja na kufanikisha matokeo kwa jumla.

Udumishaji

Kundi limeanza matumizi ya udumishaji wa ripoti na kwa sasa ile ya awali inapatikana. Ripoti hii inaadhimisha safari ya kuangazia taratibu za kudumu za utekelezaji kazi ambazo HF Group imechukua kwa muda wa miaka na kwa kusudi kundi linatumia kuimarisha biashara na mazingira.

Hitimisho

Kwa niaba ya Halshamauri, natoa shukrani zangu za dhati kwa wanahisa wetu, wateja na washirika kutokana na mchango wao usio na kifani ambao wameudhihirisha mwaka 2018. Sawia, nawashukuru wafanyakazi kutokana na uwajibikaji wao, wawekezaji kwa imani yao kwenye HF Group na wasimamizi wetu kwa mwongozo wao. Pia, ningependa kutoa shukrani kwa wanahalmashauri wenzangu kwa mwongozo wao wa kila mara na mwito wao kuangazia changamoto ambazo tunakabiliana nazo kwa muda wa miaka iliyopita.

Halmashauri imeweka hatua za kila mara zilizo makini kuangazia mikakati yetu ili kuhakikisha kwamba matokeo ya biashara yanafuata mkondo unaostahili. Kujitolea kwetu kwenu kama halmashauri kutahakisha kuwa tumefanikiwa kupita mawimbi haya na kufanikisha matokeo mazuri ya biashara. Tutazidi kuwa macho kutafuta mbinu mpya za kibiashara na kuhamasisha nafasi zaidi za ukuaji kwa kipindi kirefu kijacho.

Steve O. Mainda, EBS
Mwenyekiti wa Halmashauri
Tarehe: 28 Machi 2019

GROUP CHIEF EXECUTIVE OFFICER'S STATEMENT

Robert Kibaara
Group CEO

GROUP CHIEF EXECUTIVE OFFICER'S STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2018

Dear Shareholders,

It is my pleasure to join you for the 53rd HF Group Annual General Meeting. This is my maiden Annual General Meeting as Group Chief Executive Officer, and I am excited to be part of this financial institution with a strong heritage spanning over 53 years. I look forward to working together with my colleagues in the management team, under the aegis of the Board of Directors, to propel HF Group to deliver value for all stakeholders. Our ambition as a multidimensional financial services provider is to power the potential of all those in our ecosystem.

As management, our key mandate is to turnaround the business and as such, we have embarked on an aggressive strategy to deliver on this objective.

Expansion to new banking segments

Over the years, HF Group has built a reputation as a market leader in property development and finance. Whilst we endeavour to ring fence this strong legacy, and amplify our mortgage business, we are also augmenting our capacity in full service banking in order to diversify risk and grow our revenue streams. To this end, we now have distinct business propositions in retail, mortgage, SME, Institutional and Diaspora banking.

Building a digital bank

In 2018, we embarked on a digital transformation journey that saw the launch of a digital banking platform, HF Whizz. This is part of the business strategy to diversify and grow the retail business while addressing consumer demand for banking on the go. It is our vision that the digital banking platform will enhance our customer experience, provide comprehensive business functionality and drive profitability. So far, the business line has broken even and resulted in the

GROUP CHIEF EXECUTIVE OFFICER'S STATEMENT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2018

acquisition of over 550,000 new customers, reflecting a 600% customer growth. Majority of these customers are micro entrepreneurs, and have benefited from mobile loans and other banking and payment services available on the platform.

I am proud to let you know that within its first year, HF Whizz has already made an impact in the market place as an innovative digital banking platform, and in December 2018, HF Group won the Gold Mark and Plus One Award - Best Financial Services Sector Awards.

The Group has adopted a digital first operating model that includes digitization of operations in order to increase efficiencies and improve customer experience. We also undertook a redundancy exercise intended to streamline the business in tandem with the digital strategy implementation.

Within the period, we finalized a branch rationalisation exercise that saw the closure of Kenyatta Market and Kisii branches, bringing down the branch network to 22. This decision was informed by the investment in digital banking including virtual account opening and transaction capability to increase accessibility and customer experience through self-service.

Deepening customer relationships

Driving positive customer experience is at the centre of our initiatives and we are working to elevate our branches to customer consultation centres for financial empowerment, with well-trained employees equipped with the expertise to facilitate this. Further, the business portfolio diversification with distinct business units offering relevant value propositions for each segment is poised to deepen our relationship with customers. To ensure that we are in tune with customer expectations, we are running regular Net Promoter Score (NPS) surveys and feedback from these drives the innovations we undertake. I am pleased to note that we have made tremendous progress in this area and our NPS score has grown from -4 at the beginning of 2018 to the current +29.

Property development and mortgage financing

In 2018, the first phase of Komarock Heights consisting of 480 apartments was completed and handed over to homeowners. Richland Pointe consisting of 248 units has also been completed awaiting handover to home owners. Clay City consisting of 160 units is set for completion by end of 2019 while Precious Heights Phase 2 is due for completion in 2020. To accelerate sale of these properties and those of developers we have financed, we have kicked off a Property Sales campaign with up to 30 percent discounts on 700 properties and on boarded selling agents as part of our distribution channel.

Moving forward, the business will focus on providing mortgage financing for end buyers. The Big Four Agenda, specifically the affordable housing pillar presents a great opportunity for the business to play an active role in financing of low cost housing ownership. HF is an investor in the Kenya Mortgage Refinance Company, and as a market leader in property finance and development, we are pursuing opportunities to collaborate with partners in the public and private sector to make affordable housing a reality for Kenyans.

Financial performance

In December 2018, the Group issued a profit warning as we projected that the net earnings for the year would potentially be 25% lower than that reported for the year ended 31 December 2017. This drop in performance is attributable to two primary factors:

- Unfavourable trading environment leading to a slowdown in the real estate sector credit growth.
- The tough operating circumstances, leading to an increase in the non-performing loans position. However, we have put in place an NPL managment strategy to contain this.

Key highlights on the financial performance are as below:

- Loss before tax of Kshs 642.744 million compared to a profit of Kshs 311.624 million reported during a similar period in 2017
- Liquidity of 21.00% in 2018 up from 20.78% in a similar period in 2017
- Total Assets declined to Kshs 61 billion, down from Kshs 68 billion during a similar period in 2017 mainly due to the slowdown in lending

GROUP CHIEF EXECUTIVE OFFICER'S STATEMENT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2018

Looking ahead

The business transformation strategy we have embarked on is expected to see an improvement in perfomance in 2019, a turnaround to profitability by end of 2020 and a transformation of HF Group into a high perfomance organisation.

Conclusion

As I conclude, I would like to thank the HF Group Board of Directors for the immense support and steer they have provided to the management team as we chart the way forward for the business. I am confident that the business will bounce back and deliver value for all our stakeholders.

Robert Kibaara
Group Chief Executive Officer
Date: 28 March 2019

TAARIFA KUTOKA KWA AFISA MKUU MTENDAJI

KWA KIPINDI CHA MWAKA ULIOKAMILIKA DESEMBA 31, 2018

Kwa Wanahisa,

Ni fahari yangu kuungana nanyi kwenye halfa ya mkutano wa 53 wa pamoja wa mwaka ya HF Group. Huu ni mkutano wangu wa kwanza kama Afisa Mkuu Mtendaji na nina furaha kuwa miongoni mwa taasisi hii ya kifedha iliyo na historia ya miaka 53. Ninatarajia kufanya kazi pamoja na wenzangu kwenye timu ya usimamizi chini ya msaada wa Halmashauri ya wakurugenzi na kuiwezesha HF Group kuzalisha thamani kwa wadau wote. Lengo letu kama kituo cha utoaji huduma za kifedha za aina mbali mbali ni kuhamasisha uwezo wa wote walio kwenye mazingira ya biashara yetu.

Kama usimamizi, wajibu wetu mahsusi ni kubadilisha biashara na kwa hivyo tumerejelea mkakati ili kurudisha, kulinda na kuikuza.

Upanuzi wa huduma za benki katika vitengo vipya

Kwa muda mrefu, HF imejiwekea sifa kama kiongozi kwenye soko la ustawishaji wa raslimali na fedha. Huku tukijitolea mhanga kulinda urathi huu madhubuti na kuuvumisha, pia tunapanua uwezo wetu wa utoaji huduma kamili za benki ili kukabiliana na athari za kukuza njia zetu za mapato. Hadi kufikia sasa, tuna aina mbali mbali za biashara za kipekee kwenye soko la reja reja, chumi ndogo ndogo, taasisi na uwekezaji katika benki za nje.

Mabadiliko ya kidijiteli

Mnamo mwaka 2018, tuliendelea na safari ya mabadiliko ya dijeteli ambayo kilele chake ilikuwa kuzinduliwa kwa jukwaa la huduma za benki kupitia dijiteli-HF Whizz. Huu ni mojawapo wa mkakati wa biashara kupanua na kukuza biashara reja reja huku ikiangazia mahitaji ya watumiaji katika benki. Ni ndoto yetu kwamba jukwaa la mfumo wa dijiteli litaimarisha huduma za wateja, kutoa nafasi kubwa ya uendeshaji biashara na kuchochea faida. Hadi kufikia sasa, biashara imepanuka zaidi na kupelekea kupatikana kwa zaidi ya wateja 300,000 wapya. Wengi kati ya wateja hawa wako katika chumi ndogo na wamefaidi kutokana na mikopo ya simu tamba na huduma nyinginezo zilizoko za benki.

Ni fahari kuwafahamisha kwamba chini ya muda wa mwaka mmoja, tayari HF Whizz imeleta athari kwenye masoko kama jukwaa bunifu la kijiditeli la benki. Mnamo Desemba 2018, HF Group ilitwaa tuzo la Gold Mark na Plus One Award kwenye sekta ya utoaji huduma bora za kifedha. (Best Financial Services sector Awards).

Kundi limebuni muundo wa kwanza wa utendaji kazi kupitia mfumo wa dijiteli ambao unahusu matumizi ya kidijiteli kwenye shughuli zake kuongeza utendaji kazi na kuimarisha huduma kwa wateja. Pia, tulitekeleza shughuli ya kustaafisha wafanyakazi lengo likiwa kuweka sawa biashara kufungamana na uzinduzi wa mkakati wa kidijiteli.

Wakati wa kipindi hiki pia, tulikamilisha zoezi la kuimarisha huduma kwenye za matawi ambalo lilishuhudia kufungwa kwa tawi la Kenyatta Market na Kisii na kupelekea kupungua kwa matawi hadi kufikia 22. Hatua hii ilitokana na uwekezaji kwenye mifumo ya kidijiteli ikiwemo ufunguzi wa akaunti kupitia mtandao na uwezo wa utekelezaji ili kupanua uafikiaji wa huduma kupitia huduma za kibinafsi.

Kuimarisha ushirikiano na wateja

Kufahamu ubora wa hisia za wateja ni kiungo muhimu kwenye mikakati yrtu na tunaendelea kuboresha sura ya matawi yetu kuwa vituo vya ushauri kwa wateja na kuwapa nguvu kifedha huku tukiwa na wafanyakazi waliopewa mafunzo bora na walioimarishwa kwa ujuzi kutekeleza hili. Zaidi ya hayo, upanuzi wa biashara ukiwa na vitengo mbali mbali vinavyotoa huduma zinazohitajika kwa kila kitengo kunatarajiwa kuimarisha zaidi uhusiano wetu na wateja. Ili kuhakikisha kwamba tunaenda sambamba na mahitaji ya wateja wetu, tunaendesha utafiti wa kila mara na majibu tunayopata kutokana na zoezi hili yanaendesha ubunifu tunaotekeleza.

Ustawi wa Maendeleo na Mauzo

Awamu ya kwanza ya mradi wa Komarock Heights unaojumuisha nyumba 480 umekamilika na kutolewa kwa wamiliki wake. Mradi wa Richland Pointe wenye nyumba 248 na Clay City ulio na nyumba 160 ungali unaendelea na unatarajiwa kukamilika mwaka 2020. Ili kuhamasisha zaidi mauzo ya miradi hii na ule wa wajenzi ambao tumefadhili, tumezindua kampeini ya mauzo ya raslimali na kutoa punguko la hadi asilimia 30 kwenye raslimali 700 na kwa mawakala wa mauzo kama sehemu moja ya mbinu yetu ya usambazaji.

Agenda 4 kuu na hasa ile ya makao kwa bei nafuu inatoa nafasi kubwa ya kibiashara kwa mahitaji na usambazaji ili kutoa makao ya gharama ya chini kwa wakenya. Tumechukua hatua zinazohitajika kushauriana na wahusika serikalini kuhusu ushirikiano na wadau wa kibnafsi. HF ni mwekezaji katika Kenya Mortgae Refinance Company na kama kiongozi kwenye soko la ufadhili wa mali na maendeleo, tunatafuta nafasi za ushirikiano na washirika kwenye sekta ya umma na kibinafsi ili kufanya ndoto ya umiliki wa makao kwa gharama nafuu kuwa ya kweli kwa wakenya.

TAARIFA KUTOKA KWA AFISA MKUU MTENDAJI
KWA KIPINDI CHA MWAKA ULIOKAMILIKA DESEMBA 31, 2018

Matokeo ya fedha

Mnamo Desemba 2018, kundi lilitoa tahadhari ya faida kwani tulikadiria kwamba mapato ya jumla kwa kipindi cha mwaka yangekuwa chini ya asilimia 25 (25%) ikilinganishwa na yale yaliyoripotiwa Desemba 31, 2017. Kushuka kwa mapato haya kulichangiwa na mambo mawili muhimu:

- Mazingira yasiyo mazuri ya utekelezaji biashara yaliyopelekea kupungua kasi kwa mikopo ya ujenzi wa mitaa
- Maswala magumu ya utekelezaji ambayo yalisababisha kuongezeka kwa mikopo isiyolipika ambayo imeathiri pakubwa matokeo ya biashara. Hata hivyo, tumeweka hatua madhubuti kukabiliana na mikopo isiyolipika na tayari tumeanza mazungumzo na wateja walioathirika ili kufanya mikabata mipya kuhusiana na madeni yao.

Vidokezo muhimu kuhusu matokeo ya kifedha ni kama vifuatavyo

- Hasara kabla ya ushuru ya Kshs. milioni 642,744 ikilinganishwa na faida ya Kshs. milioni 311, 624 iliripotiwa kipindi sawa na hiki mwaka 2017.
- Mtaji wa asilimia 21 (21%) mwaka 2018 kutoka asilimia 20.78 (20.78%) kipindi sawa na hiki mwaka 2017.
- Jumla ya raslimali zilishuka hadi Kshs. bilioni 62 kutoka bilioni 68 kipindi sawa na hiki mwaka 2017 hasa kutokana na kushuka kwa utoaji mikopo.

Kuangazia siku za usoni

Kwa kuegemea mikakati ya ubunifu ambayo tumeweka, tunatarajia imariko la matokeo yetu mwaka 2019. Mkakati wa mabadiliko ambao tumerejelea umewekwa kuona kwamba kundi limerejelea faida ifikiapo mwisho wa mwaka 2020.

Hitimisho

Ninapohitimisha, ningependa kushukuru halmashauri ya wakurugenzi kwa mchango wao na mwongozo ambao wametoa kwa timu ya usimamizi huku tunapojadili mkondo wa biashara kwa siku za usoni .Tuna imani kwamba, biashara itaimarika tena na kuzaa thamani kwa wadau wetu wote.

Robert Kibaara
Afisa Mkuu Mtendaji
Tarehe: 28 Machi 2019

PICTORIAL OF ACTIVITIES

Sam Waweru, former HFC MD and Victor Lomaria, MD, Kenya Literature Bureau during the signing ceremony that will see HFC provide KLB staff with mortgages and car loans at preferential rates.

HF Group Chairman, Steve Mainda and The Arab Bank for Economic Development in Africa (BADEA) Director General, Sidi Ould during the signing of a KShs. 1.5 Billion facility.

HF Group outgoing MD, Frank Ireri (left) hands over the mantle to the new Group Chief Executive, Robert Kibaara (centre) with HF Group Chairman, Steve Mainda witnessing the handover.

HF Group leadership during the launch of HF Whizz digital banking platform in July 2018.

The HF Group team receives the Gold Mark award in recognition for Excellence in Enterprise Information Technology Adoption at the 2018 CIO 100 Awards.

HF's Chief Information Officer, George Njuguna accepts award for CIO of the year 2018 at the CIO East Africa Awards.

PICTORIAL OF ACTIVITIES

HF team, led by former HFC MD Sam Waweru (centre), pose with trophies awarded to HF Foundation by Public Relations Society of Kenya (PRSK) for "Overall Winner, PR Campaign of the Year" and "Social Investment Campaign of the Year" in November 2018.

HF Group CEO Robert Kibaara (centre) engages property agents during the launch of Shika Nyumba na HF promotion.

Buyers of Komarock Heights receive keys to their new apartments during the hand over ceremony in November 2018.

HF staff member engages with customers at Richland Pointe open day in July 2018.

HF Foundation Manager, Josephine Kirumba with three graduating interns during one of the mentorship and certification ceremonies in 2018.

HF Foundation interns graduate during one of the Foundation's mentorship and graduation ceremonies in 2018.

REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2018

The Directors have pleasure in submitting their report together with the consolidated and separate financial statements for the year ended 31 December 2018 which discloses the state of affairs of the Group and the Company.

1. Principal activities

The company is licensed as a non-operating holding company under the Banking Act (Cap.488).

The subsidiaries' principal activities are to encourage and promote the flow of both private and public savings into financing home ownership, corporate and retail banking solutions, development and selling of residential houses, insurance agency business, and social investment.

2. Results and appropriations

	2018	2017
	KShs'000	KShs'000
Gross income	**7,364,578**	**8,479,053**
(Loss)/Profit before taxation		
HF Group PLC	(97,024)	(15,899)
HFC Limited	(381,724)	373,047
HF Development and Investments Limited	(172,970)	(60,718)
First Permanent (East Africa) Limited	279	468
HF Foundation	(7,241)	(6,141)
HF Insurance Agency Limited	15,936	20,867
Group (Loss)/Profit before taxation	**(642,744)**	**311,624**
Tax	44,526	(185,408)
(Loss)/Profit after taxation	**(598,218)**	**126,216**
Retained profit and available for sale reserves brought forward	3,663,988	3,819,826
	3,065,770	**3,946,042**
Dividends – paid	(3)	(122,405)
Bonus share issue	(174,788)	-
IFRS 15 Adjustment, net of tax	(118,498)	-
IFRS 9 Adjustment, net of tax	31,935	-
IFRS 15 day 1 impact on Joint Venture (Kahawa Downs Limited) net of tax	(31,508)	-
Change in fair value of available for sale investments net of taxes	42,265	27,664
Transfer to statutory reserve	(1,528,665)	(187,313)
Retained profit and available for sale reserves carried forward	**1,286,508**	**3,663,988**

REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. Dividend

The Directors do not recommend the payment of a dividend for the financial year ended 31st December 2018. A final dividend of KShs 122,362,002 being KShs 0.35 per share was declared in the year 2017.

4. Directors

The Directors who served during the year and up to the date of this report are set out on page 4.

5. Business overview

The year 2018 experienced adverse macro-economic conditions especially reduced credit supply in the real estate sector which contributed to an increase in non-performing loans as well as slow uptake of houses ready for sale. During the year, the Central Bank rate was revised downwards twice which impacted the net interest income and overall profitability.

As a business, HF Group will focus on diversifying income streams and increasing operating efficiencies so as to deliver value to the shareholders. In this endeavour, the bank rolled out a digital banking platform (Whizz) which will boost the non interest income for the bank. In endeavour to achieve the improved performance, the Board and management have formulated the turn around strategy for years 2019 and 2020 which will propel the Group to overcome the prevailing challenges on liquidity, non performing loans and profitability. The implementation of this strategy is currently underway.

The principal risks and uncertainties facing the Group and Company as well as the risk management framework are outlined in Note 4 of the consolidated and separate financial statements.

6. Auditors

To note that KPMG Kenya have expressed their willingness to continue in office as Auditors by virtue of Section 721 (2) of the Companies Act, 2015.

7. Relevant audit information

The Directors in office at the date of this report confirm that:

- There is no relevant audit information of which the Company's auditors are unaware; and
- Each director has taken all the steps that they ought to have taken as a director so as to be aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

8. Approval of financial statements

The financial statements set out on pages 74 to 169 were approved and authorised for issue at a meeting of the directors held on 28th March 2019.

BY ORDER OF THE BOARD

Regina Anyika
Company Secretary

Date: 28 March 2019

RIPOTI YA WAKURUGENZI
KWA KIPINDI CHA MWAKA ULIOMALIZIKA DESEMBA 31, 2018

Wakurugenzi wanafuraha kutoa ripoti yao pamoja na taarifa zilizowekwa pamoja na taarifa nyingine za matumizi ya pesa kwa kipindi cha mwaka uliomalizika Desemba 31 2018 ambazo zinafichua hali ya kundi na kampuni.

1. Shughuli Muhimu

Kampuni hii imesajiliwa rasmi Kama kampuni isiyoshikilia pesa za wateja chini ya kifungu cha sheria za masuala ya benki (nambari 488)

Shughuli nyinginezo ndogo ni pamoja na kuhimiza na kuhamasisha uwekaji wa akiba wa kibinafsi na wa umma kufadhili umiliki wa makao, na suluhu la benki kwa mashirika na huduma za reja reja, kujenga na kuuza nyumba za kuishi na uwakala wa biashara za bima pamoja na uwekezaji wa kijamii.

2. Matokeo na Makadirio

	2018	2017
	KShs'000	KShs'000
Mapato kwa jumla	**7,364,578**	**8,479,053**
(Hasara)/ Faida kabla ya ushuru		
HF Group PLC	(97,024)	(15,899)
HFC Limited	(381,724)	373,047
HF Development and Investments Limited	(172,970)	(60,718)
First Permanent (East Africa) Limited	279	468
HF Foundation	(7,241)	(6,141)
HF Insurance Agency Limited	15,936	20,867
(Hasara)/Faida ya kundi kabla ya ushuru	**(642,744)**	**311,624**
Ushuru	44,526	(185,408)
(Hasara)/Faida baada ya ushuru	**(598,218)**	**126,216**
Faida illiyohifadhiwa na iliyo tayari kuuzwa na hazina zilizowasilishwa	3,663,988	3,819,826
	3,065,770	**3,946,042**
Mgawo-uliolipwa	(3)	(122,405)
Mgawo wa hisa za ziada	(174,788)	-
Mabadiliko ya IFRS 15, baada ya ushuru	(118,498)	-
Mabadiliko ya IFRS 9, baada ya ushuru	31,935	-
Athari za IFRS 15 kwa siku ya kwanza (Kahawa Downs Limited) baada ya ushuru	(31,508)	-
Mabadiliko ya thamani kwa rasilimali zilizoko kwa mathumuni ya kuuzwa na ushuru kwa jumla	42,265	27,664
Uhamisho kutoka kwa hazina ya kisheria	(1,528,665)	(187,313)
Faida iliyohifadhiwa na iliyoko kwa madhumuni ya mauzo yaliyowasilishwa mbele	**1,286,508**	**3,663,988**

RIPOTI YA WAKURUGENZI
KWA KIPINDI CHA MWAKA ULIOMALIZIKA DESEMBA 31, 2018

3. Mgawo wa Faida

Wakurugenzi wanatoa pendekezo la malipo ya mwisho ya mgawo wa faida wa Kshs.0 (mwaka 2017 ilikuwa Kshs. 122, 358,833). Malipo ya awali ya mgawo wa faida yaliyofikia Kshs. 0 (2017 yalikuwa 0) yalitolewa wakati wa kipindi hiki cha mwaka. Kwa hivyo, jumla ya mgawo wa faida ni Kshs.0 (2017 yalikuwa Kshs. 0.35) ambayo yamefikia kima cha Kshs.0 (2017 yalikuwa Kshs. 122,358,833).

4. Wakurugenzi

Wakurugenzi waliohudumu wakati wa kipindi hiki cha mwaka wameangaziwa kupitia ukurasa wa kwanza.

5. Mtazamo wa biashara:

Mwaka 2018 ulishuhudia mabadiliko makubwa katika sekta ya chumi ndogo hasa kupunguzwa kwa utoaji mikopo kwenye sekta ya ujenzi wa mitaa ambayo ilisababisha kuongezeka kwa mikopo isiyolipika. Wakati wa kipindi cha mwaka, kiwango cha riba kilifanyiwa mabadiliko na kwenda juu maradufu hali iliyoathiri mapato ya jumla na faida kwa jumla.

Kama biashara, Benki ya HF Group itaangazia kubuni mbinu mbali mbali za mapato, vile vile kuimarisha utendaji bora wa shughuli ili kuwezesha matokeo yenye thamani kwa washikadau. Katika jitihada hizi, benki hii ilizindua jukwaa la kidijitali la kutoa huduma za benki (Whizz) litakalothibitsha mapato ya benki yasiyo na riba. Ili kuimarisha matokeo, Bodi na usimamizi zimeunda mkakati wa kubadilisha mwelekeo katika mwaka wa 2019 na 2020, utakaosaidia benki hii kukabili changamoto zilizopo za kusarifika, mikopo isiyo na riba na faida. Shughuli za kutekeleza mkakati huu ziko mbioni.

Hatari kuu na taharuki zinazokabili kampuni na kundi pamoja na mbinu za usimamizi ili kujihami kukabiliana na hatari zimeelezewa kupitia nukuu ya nne ya taarifa ya pamoja na iliyotengwa ya matumizi ya pesa

6. Wakaguzi wa pesa

Kutambua kwamba wakaguzi wa pesa KPMG Kenya wataendelea na jukumu lao kwa mujibu wa sehemu ya 721 (2) ya sheria za makampuni ya mwaka 2015.

7. Maelezo muhimu ya ukaguzi wa pesa

Wakurugenzi wanaohudumu kipindi hiki cha tarehe hii wanathibitisha kwamba:

- Hakuna maelezo yoyote muhimu ambayo wakaguzi wa pesa za kampuni wasiyoyafahamu; na
- Kila mkurugenzi amechukua hatua zinazohitajika kuchukuliwa kama mkurugenzi kufahamu maelezo yoyote ya uhasibu yanayofaa na kufahamu kwamba wakaguzi wa kampuni wanafahamu maelezo hayo.

8. Kuidhinishwa kwa taarifa za matumizi ya pesa

Taarifa za matumizi ya pesa zilizofafanuliwa kupitia ukurasa wa 74 hadi 169 ziliidhinishwa wakati wa mkutano wa wakurugenzi uliofanyika 28 Machi 2019.

KWA AMRI YA HALMASHAURI

Regina Anyika
KATIBU WA KAMPUNI

Tarehe: 28 Machi 2019

DIRECTORS' REMUNERATION REPORT
FOR THE YEAR ENDED 31 DECEMBER 2018

HF Group PLC (the "Group") is pleased to present the Directors' remuneration report for the year ended 31 December 2018. This report is in compliance with the Group's remuneration policy, CMA Code of Corporate Governance Guidelines on Directors' remuneration and the Companies Act,2015. The remuneration is reviewed regularly to ensure that it is within the existing market rates. This is done to ensure that individual member (director) is effective and continue to pursue the business strategy. Performance of each member is evaluated annually and communicated appropriately. All members are expected to observe attendance of the board meetings and make valuable contributions depending on each member's area of speciality. The remuneration is disclosed through the periodic publications made by the Group.

During the financial year, the Group's Board of Directors consisted of:

Frank Ireri	- Outgoing Group Managing Director
Robert Kibaara	- Group Chief Executive Officer
Steve O. Mainda	- Chairman
Benson I. Wairegi	
Peter K. Munga	
Adan D. Mohamed	
Constance Gakonyo	
Kaushik Manek	
Felister Kembi	
Gladys Karuri	

The remuneration of the executive director is as per negotiated employment contract. There has been no change to the non-executive directors' remuneration, as approved by the shareholders on 29 April 2016.

DIRECTORS' REMUNERATION REPORT (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2018

For the financial year ended 31 December 2018, remuneration and other incentives for the Board was as summarized below:

Non- Executive Directors

	2018 KShs'000			2017 KShs'000		
Name	**Fees**	**Sitting Allowance**	**Total**	**Fees**	**Sitting Allowance**	**Total**
Dr. S.O. Mainda	4,847	-	4,847	5,199	-	5,199
Dr. Benson Wairegi, EBS	488	1,664	2,152	488	1,300	1,788
Dr. Peter K. Munga	488	936	1,424	488	704	1,192
Adan D. Mohamed	648	1,248	1,896	648	1,872	2,520
Constance Gakonyo	488	1,300	1,788	488	1,040	1,528
Kaushik Manek	488	1,248	1,736	488	1,040	1,528
Felister Kembi	488	780	1,268	488	572	1,060
Gladys Karuri	488	728	1,216	488	572	1,060
	8,423	**7,904**	**16,327**	**8,775**	**7,100**	**15,875**

Executive Director (Frank Ireri)	**2018**	**2017**
	Kshs. '000	**Kshs. '000**
Basic Pay	44,105	44,476
Non-Cash Benefits	6,247	6,150
Gratuity	13,787	13,787
Total	**64,139**	**64,413**

Aggregate loans to directors and senior management amounted to KShs. 251,653,320. The Group will not be proposing to make any changes to the executive and non-executive directors' remuneration level during the current financial year.

DIRECTORS' REMUNERATION REPORT (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2018

Non-Executive Directors' remuneration policy and framework

Non-Executive Directors are engaged on the basis of a letter of appointment. It is the policy of the Board of Directors that Non-Executive Directors are paid directors' fees and sitting allowances, but are not eligible to participate in any of the Company's bonus, share option or pension schemes.

Details of the policy on fees paid to our Non-Executive Directors are set out in the table below:

Directors Fees & Sitting allowances (Cash)	Policy framework
To attract and retain Non-Executive Directors of the highest calibre and having the necessary skills and expertise to exercise independent judgement on issues that promote the company's objectives.	The directors fees and sitting allowances paid to Non-Executive Directors are determined by the Board of Directors, with recommendations from the Group Nomination and Governance Committee.
	Members of the various Committees are also eligible to receive an additional sitting allowance fee.
	The fees payable are reviewed periodically by the Group Nomination and Governance Committee to ensure that the fees remain competitive and in line with remuneration of other non-executive directors in the same industry. Time commitment and responsibility are also taken into account when reviewing fees.
	Travel and expenses for Non-Executive Directors (including the Chairman) for company related assignments are all met by the Company.

Approval of the director's remuneration report

The Directors confirm that this report has been prepared in accordance with the Kenyan Companies Act, 2015, Capital Markets Authority (CMA) Code and listing rules and reflects the disclosure requirements under IFRS.

BY ORDER OF THE BOARD

Regina Anyika
Company Secretary

Date: 28 March 2019

CORPORATE GOVERNANCE
FOR THE YEAR ENDED 31 DECEMBER 2018

HF Group PLC is commited to good corporate governanace practices to achieve effective and responsible leadership characterised by ethical values of responsibility, accountability, fairness and transparency. Board and management have ensured compliance with the Cental Bank guidelines on corporate governanace (CBK/PG/02), Capital Markets Authority Code of Corporate Governance Practices for Issuers of Securities to the Public, 2015 and internationally accepted principles and best practices in corporate governance. We consistently review these practices to ensure that the best interests of our stakeholders are always acted upon.

HF Group board approved a corporate governance policy detailing the key corporate governance practices applicable to the group as well as all main subsidiary companies. The policy sets out the Corporate Governance Framework for guidance to the Board and management by defining key responsibilities as well as ethical standards expected of them.

1. The Board of Directors

The board has ultimate accountability and responsibility for the performance and affairs of the Group by providing leadership and strategic guidance to sustainably safeguard stakeholders' value. The HF Group PLC board has the following responsibilities:

- Approving the group strategy and continually monitoring management's performance and implementation of the strategy;
- Ensuring that adequate financial and capital resources are in place for the Group to meet its strategic objectives;
- Ensuring that the group has appropriate risk management systems and policies to effectively control and report on all key risk areas and key performance indicators of the business.

The board operates under a formal charter that is regularly reviewed, a copy of which can be accessed at www.hfgroup.co.ke. The Board has a formal schedule of the meeting in which notices and agenda are circulated to all Directors on a timely basis together with the respective documents for discussion.

Composition of the Board

The Board determines its size and composition, subject to the group's Articles of Association, Board Charter and applicable law. Currently, the Board is composed of the Group Chief Executive Officer and eight non-executive Directors, five of whom are independent, including the Chairman. The Directors have a wide range of skills and experience and each contributes independent judgement and knowledge to the Board's discussions.

On appointment, each Director is provided with a comprehensive and tailored induction process covering the Group's business and operations and provided with information relating to their legal and regulatory obligations.

All non-executive Directors are required to submit themselves for re-election in accordance with the Company's Articles of Association.

Conflict of interest

Directors are prohibited from using their positions, or confidential and price-sensitive information, for their own personal or related third-party benefits. Directors are required to disclose to the board of any or potential conflicts of interests that they may have in relation to particular items of business. A register of individual directors' interests in and outside the company are maintained and updated with details noted by the board on regular basis.

CORPORATE GOVERNANCE
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

1. The Board of Directors (Continued)

Procedure for nomination of Directors

The Nomination and Governance committee is responsible for proposing to the Board qualified candidates that meet the criteria to serve as directors and board members of board committees. The committee uses a board skill matrix to determine the knowledge, capabilities, expertise and experience required for any vacancy. In case of directors representing a major shareholder, the shareholders nominates individuals to be elected as directors while the board verifies their qualifications.

The Nomination and Governance committee scrutinises the qualifications of each candidate and proposes the selected candidate for nomination to the board for consideration. Following the board's endorsement of the nominated candidate, a letter of no objection is sought from Central Bank of Kenya before proposing nomination by shareholders.

2. Board Committees

The HF Group Plc board constituted three committees to assist the board in the discharge of its duties and responsibilities. Each board committee has formal written terms of reference that are reviewed on annual basis. The committees include the Nomination and Governance, Audit & Risk and Strategy.

(a) Nomination and Governance Committee

The members of the Nomination and Governance committee are:

- Constance Gakonyo (Chairperson)
- Peter Munga
- Gladys Ogallo
- Robert Kibaara (Group Chief Executive Officer)

Majority of the committee members are Non-Executive Directors with chair being independent non-executive director. The committee operates under board approved Terms of References and meets at least on a quarterly basis.

The Committee's responsibilities include:

- Reviewing the structure, size and composition of the Board to ensure the optimum balance of skills, knowledge and experience taking into account the opportunities and challenges which face the Group;
- Identifying and nominating for the approval of the Board a suitable candidate for any Board vacancy which may arise;
- Monitoring the development of succession plans for the Group relating to senior executive management;
- Reviewing the emoluments of both executive and non executive Directors, and senior management.

This Committee carries out a peer and self-evaluation of the Board and its committees to assess their contribution and also to ensure that there is the requisite mix of skills and experience available to effectively discharge their duties.

CORPORATE GOVERNANCE
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

2. Board Committees (continued)

(b) Board Audit & Risk Committee (BARC)

This committee is composed of four Non-Executive Directors and operates under board approved Terms of References.

- Felister Kembi (Chairman)
- Adan D. Mohamed
- Kaushik Manek
- Gladys Karuri

Majority of the committee members are independent Non-Executive Directors including the Chair. Two members of the committee are qualified accountants and are members of the Institute of Certified Public Accountants of Kenya (ICPAK). The committee operates under board approved Terms of References and meets at least on quarterly basis.

The principal roles of the committee are to:

- Ensure that accounts are prepared in a timely and accurate manner to facilitate prompt publication of annual accounts;
- Review the internal controls, including the scope of the internal audit programme, the internal audit findings and recommend actions to be taken by management.
- To review and assess the integrity of the risk control systems and ensure that the risk policies and strategies are effectively managed.
- Monitor compliance with applicable law, statutory and regulatory requirements.
- Nominate external auditors for appointment by the shareholders
- Review of any related party transactions that may arise within the group.
- Monitor the external auditors' independence and objectivity, taking into consideration relevant professional and regulatory requirements.

(c) Board Strategy Committee

This committee is composed of six Non-Executive Directors and the Group Chief Executive Officer:

- Benson Wairegi (Chairman)
- Peter K. Munga
- Adan D. Mohammed
- Gladys Ogallo
- Kaushik Manek
- Gladys Karuri
- Robert Kibaara (Group Chief Executive Officer)

CORPORATE GOVERNANCE

FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

2. Board Committees (continued)

(c) Board Strategy Committee (Continued)

The principal roles of the committee are to:

- Oversee the implementation of the Group's strategy;
- Approve and participate in the annual strategy review process;
- Approve all key strategic initiatives including but not limited to; appointment of consultants, capital & revenue expenditure and investments.

Attendance of Individual Directors

The following table shows the number of Board meetings held during the year and the attendance of individual Directors:

Board meetings attendance for the year ended 31 December 2018	**Board meetings**			**Total attendance**	
Date	27-Feb	24-Apr	25-May	24-Oct	
Steve Mainda	√	√	√	√	4
Frank Ireri	√	√	√	X	3
Benson Wairegi	√	√	√	√	4
Peter Munga	√	√	√	√	4
Adan Mohamed	X	√	√	√	3
Constance Gakonyo	√	√	√	X	3
Kaushik Manek	X	√	√	√	3
Felister Kembi	√	√	√	√	4
Gladys Karuri	√	√	√	√	4

√ Attended
X Absent with apology
N/A Not applicable

A number of Management committees have been established by the Board to oversee operations in some critical areas. These are Executive committee (EXCO), Asset and Liability committee (ALCO), Risk Management committee, Lending committee, Arrears Management committee, Information Technology Steering committee and Management Strategy committee (STRATCOM). The Board appoints other committees as and when necessary.

CORPORATE GOVERNANCE
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. Board effectiveness evaluation

To assess the performance of the Board, its committees and individual Directors, the Board conducts a rigorous performance evaluation each year. The process is led by the Chairman and supported by the Company Secretary.

In March 2019, the Directors completed the annual evaluation that covered a self-evaluation, evaluation of the Chairman and the overall Board. The conclusion of the evaluation was that the Board operated effectively. The results of the evaluation were submitted to the Central Bank of Kenya.

The Nomination & Governance Committee approved an evaluation process for non-executive Directors, which entails conducting one to one meetings with the Non-Executive Directors to discuss their performance and contribution.

4. Internal audit function

HF Group has designed an internal control system to ensure the integrity and reliability of financial statements and nonfinancial reporting as well as compliance with laws and internal standards and policies.

The Group has a fully operational internal audit function headed by a qualified senior staff member with functional reporting line to the Group Board Audit & Risk Committee. The function forms the third line of defence within the group enterprise risk management framework. The purpose of the audit function is to provide independent and objective assurance to the board that the governance processes and systems of internal control are adequate and effective. The audit function operates under annual risk based audit plan taking into considerations specific regulatory requirements and approved by the board audit committee.

5. Risk Management

The ultimate responsibility of the group's risk management rests with the group board of directors. The board is assisted by the Board Audit & Risk Committee with an independent Risk Management and Compliance function, which reviews the adequacy of the risk management systems and reports independently to the committee.

The group has instituted an enterprise risk management framework designed to identify, evaluate and manage significant risks associated with the achievement of the group's objectives.

6. Whistle Blowing Policy

HF Group has a whistleblowing policy that has multiple reporting lines including through an independent and credible external party. HF Group staff, customers and general public are encouraged to make reports on unethical and fraudulent behaviours without fear of retaliation from the suspected individuals.

All reported cases are promptly and comprehensively investigated with meritable actions being taken against identified culprits. A summary report is presented to the Board Audit Committee on a quarterly basis.

7. Communication with shareholders

The Group is committed to:

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

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

8. 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 10 to the financial statements.

CORPORATE GOVERNANCE
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

9. Major shareholders as at 31 December 2018

	Name	No. of shares	% age shareholding
1	BRITAM HOLDINGS PLC	74,666,146	19.41
2	EQUITY NOMINEES LIMITED A/C 00104	48,828,477	12.70
3	BRITAM LIFE ASSURANCE COMPANY (KENYA) LTD	35,891,083	9.33
4	BRITAM LIFE ASSURANCE COMPANY (KENYA) LTD	25,597,000	6.66
5	STANDARD CHARTERED NOMINEES RESD A/C KE11401	15,622,569	4.06
6	PERMANENT SECRETARY TREASURY	9,265,135	2.41
7	KERAI, RAMILA HARJI MAVJI & HARJI MAVJI	6,202,500	1.61
8	MWANGI,PETER KINGORI	5,512,219	1.43
9	KIBUWA ENTERRPRISES LIMITED	5,012,575	1.30
10	KCB NOMINEES LTD A/C 915 A	4,322,023	1.12
	TOTAL	**230,919,727**	**60.03**

10. Distribution of shareholders as at 31 December 2018

Number of shares	No. of shareholders	No. of shares held	% age shareholding
1-500	7,445	1,450,087	0.38%
501-1,000	4,470	2,962,832	0.77%
1,001-10,000	13,586	37,192,979	9.67%
10,001-50,000	1,456	28,199,731	7.33%
50,001-100,000	179	12,411,191	3.23%
100,001-1,000,000	143	35,421,859	9.21%
Over 1,000,000	23	266,975,489	69.41%
TOTAL	**27,302**	**384,614,168**	**100.00%**

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT

HF Group presents its 2018 Sustainability Report. For the first time, HF Group has collected all relevant non-financial information on its environmental, social, governance and ethics, and economic impact in one standalone report. This marks the start of our journey as we progress in our commitment towards more responsible and sustainable business practices.

This abridged version of the report forms part of the annual report for the first time this year.

Please visit our website, **www.hfgroup.co.ke**, to find the full report, our archived corporate citizenship reports and additional information regarding HF Group and our sustainability journey. If you have any questions or comments about our report, feel free to email us at **sustainability@hfgroup.co.ke**

Scope and Boundary of the Report

This report presents data for 2018, accompanied by prior-year results for context. It has been prepared in accordance with the **GRI Standards: Core option**. We have not sought any external assurance for this report.

We provide information on our economic, environmental, and social performance of all HF Group subsidiary companies from the perspective that we believe are useful to our stakeholders. For this first report, most of the references are for HFC and HFDI, our largest business segments. We believe the information is representative of all our Group entities.

As we continue to advance our data collection and reporting processes, we will be able to present more accurate and comprehensive information.

About our Sustainability Creation Journey

The Sustainability Creation Journey is our plan to make a difference for our people, in our communities, and for the environment.

In 2018, we began the process of identifying the strategic commitments that will drive a sustainability vision across the Group. These commitments will enable a heightened focus on measurement and will be linked to our employee performance incentives. We have identified the following corporate priorities for addressing sustainability issues and opportunities across our entire business i.e. maintain accurate and comprehensive sustainability reporting

1. Leverage sustainability to grow the business
2. Embed sustainability in our performance management
3. Promote sustainability throughout our value chains
4. Increase global leadership and policy engagement

Stakeholder Engagement

A cross-functional team of 25 staff members underwent two sustainability-training sessions in 2018. These Sustainability Champions worked with **MK-Africa** Consultants to evaluate our significant sustainability issues. These issues generally fall into the broad categories outlined in this report. We will update our materiality assessment in the coming months to include diverse stakeholder perspectives.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

STAKEHOLDER GROUP	DESCRIPTION
Customers	1. HFC - 331,811 customers 2. HFDI –1,038 households 3. HF Foundation – 4,954 beneficiaries 4. HF Insurance Agency – 6,418 customers 5. First Permanent EA Limited – non-trading company
Employees	1. Long-term employees - 385 2. Short-term employees - 19
Regulators	1. Central Bank of Kenya 2. National Treasury 3. Capital Market Authority 4. Nairobi Securities Exchange 5. Kenya Bankers Association 6. Insurance Regulatory Authority 7. Retirement Benefits Authority
Investors	1. Shareholders 2. Fund managers 3. Analysts
Communities	1. Foundation Beneficiaries 2. Media 3. Advocacy Groups

Business Success Factors

In 2018, we carried out an online survey where we got the views of more than 100 staff and customers. We also interviewed the Group's senior executives to define the business success factors to include in our materiality analysis. These were defined as:

1. **Technology & Innovation** - Creation of new industry-leading products & services that remain aligned to customers' expectations and needs.
2. **Economic Performance** - Growth, profitability, capital efficiency and risk exposure.
3. **Governance and Regulatory Compliance** - Complying with applicable regulatory requirements to promote high standards of business ethics, working against corruption, extortion and bribery, payment of tax contributions in accordance with legislative requirements and a transparent approach to financial reporting. Also establishment of an ethical culture, leading with integrity and being socially responsible
4. **Providing Quality and Affordable Housing** - Building high-quality homes, providing the best service for our customers and engaging with the local communities to help us create developments that reflect local needs and add value to the community
5. **Transparency, Accountability and Responsible Marketing (Publicity)** - Openly disclosing strategic sustainability approach and performance against measurable targets, as well as marketing products & services honestly and avoiding negative implications for the customer and end user.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

Strategic Sustainability Objectives

Environmental 1

Introduce long-term environmental goals for the reduction for waste, energy and greenhouse gas (GHG) emissions associated with our operations at corporate and branch level.

Social 2

1) Maintain a productive, supportive and safe working environment.
2) Offer innovative products and services relevant to our customers.
3) Actively participate in improving financial inclusion for youth in Kenya.

Economic 3

1) Deliver value for customers, shareholders, and stakeholders in a responsible manner.
2) Report on our actions and results transparently.
3) Increase the efficiency of our value chain.

Governance & Ethics 4

Promote ethical principles and good corporate governance throughout our business ecosystem.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

Strategic Sustainability Objectives

We expect our updated materiality assessment and stakeholder engagement to lead to applicable sustainability objectives and targets. In the coming months, these will be incorporated into collective and individual staff performance management and evaluations. By the end of 2019, all staff will have at least one relevant sustainability-related key performance indicator with corresponding target included in their performance scorecards. These individual indicators will further feed into our overall department and management performance indicators.

Our approach to the Sustainable Development Goals (SDGs)

In 2018, we identified the five SDGs below as core to our operations. In the coming months, the Group will have internal stakeholder discussions to articulate how our commitment to sustainability fits within our business strategy and make specific contributions towards each of the selected SDGs.

GOVERNANCE, ETHICS AND COMPLIANCE

(a) Corporate Governance

The top governance body at HF is the Board of Directors. Eight of the nine members are non-executive directors. There are 3 board committees that are all chaired by non-executive directors. The Board and the committees perform annual self-evaluations. The Board is composed of three women and six men; all the directors are Kenyan and over 45 years of age. Diversity is one of the factors we take into consideration in placing new directors on the board.

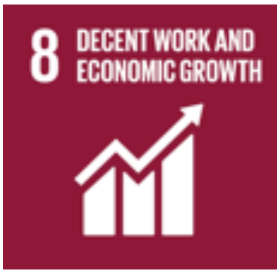
The Nominations & Governance Committee of the Board of Directors reviews the structure, size and composition of the Board, identifies suitable candidates to fill in board vacancies, develops succession plans for the board, sets performance criteria and compensation for the CEO, and also reviews and approves compensation for other executive officers.

The HF Executive Committee includes 12 senior managers representing all major operational and administrative groups within HF Group. The EXCO supports the Board of Directors in executing HF strategy. The only member of the EXCO to sit on the Board of Directors is the Group CEO. The EXCO is composed of seven men and five women; all are Kenyan.

(b) Ethics

Our fundamental commitment to ethics is reflected by the strong infrastructure that surrounds it. We have a clearly defined Code of Ethics, which sets our expectations of employees, leaders and business partners.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)



We have enhanced our Code of Ethics to include sexual harassment and whistle blowing policies with a view to creating decent working conditions for all our employees. We will be looking to develop these policies as we reach out to include the key stakeholders in our value chain.

Target Actions in 2019

1. **Training**: Full-time management employees will complete comprehensive training on compliance and ethics programs every 2 years. This will include training on our Code of Ethics as well as participating in our business ethics questionnaire.
2. **Supplier Code of Conduct:** Develop a Supplier Code of Conduct consistent with our Code of Ethics.
3. **Ethics Advocates:** Identify ethics advocates at our branches help to ensure that our stakeholders understand and live by the HF Code of Ethics.

Our Whistle Blowing Policy outlines the course of action that our stakeholders should to take in instances where they suspect improper, unethical or inappropriate conduct in the course of our business.

There were 7 cases reported in 2018. Proper investigations were conducted and appropriate actions taken by the concerned departments. All of the codes and policies discussed in this section, and related documentation are available on our website.

ENVIRONMENT

(a) Environmental Sustainability

Our Environmental & Social Risk Policy, (February 2017) guides our commitments to environmental protection across all group subsidiaries. HF Group views environmental sustainability from two perspectives:

1. We conduct business in a manner that protects our employees, the communities where we operate and the environment; and
2. We offer products and services that deliver efficiency contributing to an overall reduction in the usage of natural resources.

The Environmental and Social Risk policy has been incorporated into our lending process and is aligned with IFC Performance Standards. Our loan application therefore includes, among other issues, an environmental assessment. In compliance with requirements of the National Environment Management Authority (NEMA), all our HFDI projects undergo Environment Impact Assessment (EIA) before construction begins. All our sites are NEMA compliant.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

Green building technology refers to the application of processes that are environmentally responsible and resource efficient throughout a building's life cycle: from planning to design, construction, operation, maintenance, renovation and demolition. As a company committed to global standards, HFDI has incorporated green or sustainable building technology in our most recent developments including Richland Dam Project, Komarock Heights and Precious Gardens phase 1 & 2.

(b) Product Footprint and Lifecycle Thinking

Our implementation of cloud infrastructure in 2018 has led to an increase in energy efficiency and improved processes. It has also enabled reduction in our carbon footprint.

We are committed to reusing and recycling materials where possible. The Group has been able to save up to Kshs. 214,000 on toners, printing papers and electricity. In the coming months, we are looking to start Digital Archiving, which will lead to automation of our registry. We are also looking into online validation of cheques. This will improve efficiency in the processing of cheques and reduce printing of physical cheques thus enabling the bank to save on paper and electricity.

In 2018, HFC invested in digital banking platforms with the roll out of a new interactive website, online banking and a mobile app. This gives customers control and access to their accounts anywhere and anytime. HFC was awarded the best emerging digital innovation in 2018.

At HFDI, our long-term strategy is to fully incorporate green construction or sustainable buildings. We are also looking to increase our efforts for the environmental restoration of degraded sites, reduce the amount of waste at our sites, continue to carry out Environmental Impact Assessments (EIAs) for proposed projects and perform initial environmental audits for completed projects.

Target Actions in 2019

1. Assess our corporate environmental footprint and measure our $CO2$ emissions.
2. Increase our investment in digital banking platforms to reduce our overall carbon footprint.
3. Continue to incorporate green building technology within our HFDI portfolio.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

SOCIAL

(a) Workplace Health and Safety

Maintaining the health and safety of our employees, customers and neighbors, and protecting the environment are part of our corporate philosophy. Our objective is to have zero accidents, zero errors and zero harm. We are committed to publicly reporting our safety statistics as part of our sustainability strategy. Our safety statistics in recent years highlight our commitment to the safety of our employees. We have a permanent Health and Safety officer at each of our HFDI sites to ensure incidences are reported and addressed immediately and compliance by the workforce to set guidelines on the protective equipment. Over the last seven years, zero fatalities have been recorded in our sites. We will continue to track our injury reporting and use the data collected to improve safety.

(b) Product Safety

Regulatory compliance is a top priority for us. Our approach is to: Employ a management system to evaluate and communicate product safety, comply with all regulatory requirements for our product development and marketing and maintain open and constructive dialogue with internal and external stakeholders on our products. We have a policy which prohibits lending to institutions that may lead to the increment of social vices. This includes but not limited to gambling companies.

(C) Employee Attraction, Engagement and Retention

We are proactive and progressive in our human resources policies and our programs and are committed to creating an outstanding place to work and build a career. We have key policies and provisions support our strong viewpoints on diversity and inclusion, anti harassment and human rights. We also invest in talent development through workshops and training programs. In 2018, a total of 119 employees were trained. Of these, 15 were managerial staff and 104 were technical/professional staff. The training mainly focused on leadership development.

Our policies also support our commitment to providing company benefits, from health coverage to bereavement leave. We have business resource groups, such as the HF Women's Group, which are employee-led initiatives. Among the group's activities in 2018 include organizing a series of talks and presentations to our women staff through an initiative dubbed – Inspiring Women at the work place. There is room for improvement. Our last employee engagement survey was carried out in 2016 where 184 employees participated to give us an average rating.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

We have made deliberate efforts to promote women in technology. We have increased the number of women working in our ICT department from none in 2016, 15% in 2017 and 20% in 2018. Women in senior management positions from job grade M2 and above as a percentage –35%.

2018 Employee Highs & Lows

1. In July 2018, HF Group laid off 36 employees. This was intended to streamline the business in tandem with the digital strategy implementation. Employees who were laid off received pay in lieu of notice. The Central Bank of Kenya, Capital Markets Authority and the Ministry of Labour and Social Protection were all notified according to statutory requirements.
2. We also realigned our business segments to more clearly reflect our evolving business model and we become a fully-fledged financial institution.
3. In December 2018, Robert Kibaara began serving as HF Group Chief Executive Officer, succeeding Frank Ireri's planned retirement. Robert Kibaara was previously Director for Retail Banking at NIC Bank.

(d) Community Involvement - The HF Foundation's Army of One Million Artisans

HF Foundation (HFF) is the company's social investment arm. Its focus is to facilitate technical skills training guided by its vision of the creation of 'an army of one million artisans' for the building and construction industry in Kenya. Since inception in 2012, HFF has supported and engaged 4,954 interns in our intensive mentorship program. In 2018, the foundation had 282 interns.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

1. In 2014, HFF launched the Competency Based Education and Training (CBET) curriculum framework development in partnership with industry, technical training institutions, Ministry of Education Science and Technology, TVET Authority, National Construction Authority and other local and international partners. This was the first of its kind in technical skills training in Kenya. Ten (10) Occupational Standards for the building and construction industry were completed in 2016 and handed over to the Curriculum Development, Accreditation and Certification Council (CDACC) and the National Industrial Training Authority (NITA) for development into curricular for use in Technical Training Institutions.

2. A training program for instructors from Technical Training Institutions on CBET Curriculum delivery was conducted in 2015. Participants were 30 Technical Training Instructors from across the country.

3. A skills enhancement program was undertaken in partnership with the company, Alibhai Shariff, in 2015 and 2016. 980 artisans participated in experiential learning on the use of modern technology for their trade.

4. HFF's "TVET on Wheels" training program, in partnership with Kiambu Institute of Science and Technology (KIST), takes place at our construction sites. Skills acquired are applied in real time. 853 young people have undertaken this program with 252 successfully completing the program.

5. In 2017, HFF partnered with GIZ -4ED SOGA internship program. This is a program aimed at equipping building and construction technicians and artisans with necessary skills required for the building and construction Industry. To date it has supported a total of 477 interns and 1 instructor.

In 2018, HF Foundation was awarded the overall winner of two (2) Public Relations Society of Kenya awards:

- PR Campaign of the Year Award
- Social Investment Campaign of the Year

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

Target Actions in 2019

- Employee survey - In order to measure and understand our employees' attitude, feedback, motivation, and satisfaction.
- Integrated Flexible Environment: Work arrangements such as flextime, reduced hours and ad hoc telecommuting. These will include parental benefits in line with best practice and, provide competitive options for employees who are new parents.
- SDGs aligment: Link the work we are doing with TVETs with our alignment with the Sustainable Development Goals (SDGs)

ECONOMIC

(a) Economic Sustainability

2018 saw us report an unsatisfactory financial performance. We are however committed to using our financial resources responsibly. Our economic value creation will be driven by our increasing investment in digital products and services to make us efficient with our resources. Also as a leading integrated solutions enabler in the property industry, we will continue to offer innovative products and services across the property value-chain as suppliers and financiers. Our financial goals and performance are documented extensively online and in our 2018 Annual Report (www.hfgroup.co.ke/investor-relations).

Economic Highs and Lows in 2018

1. In July 2018, we launched a new mobile banking platform, HF Whizz, as part of our turnaround strategy targeting investment in digital and retail banking. The platform aims to enhance customer experience, provide comprehensive business functionality and drive profitability.
2. We declared a loss of KShs. 637M as at December 2018.
3. As at December 2018, we paid out Ksh. 395 million in interest payments to HF bondholders. The payout was on the KShs. 3Bn corporate bond issued six years ago.
4. The banking sector has been grappling with reduced profit margins after amended laws capped the cost of loans. In November 2018, we issued a warning anticipating lower full year profit with interest income being 25 percent lower than 2017.
5. In December 2018, our stock fell to below par value on the Nairobi Securities Exchange. This 15-year low has weighed down on investor sentiment and also saw our key shareholder, Britam, lose nearly KShs. 4Bn in paper wealth.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

Financial Focus (in thousands except per share amounts)

	2018 Kshs' 000	2017 Kshs' 000
Revenue	7,364,578	8,479,052
Operating expenses	(8,007,322)	(8,167,428)
Net income	(642,744)	311,624
Adjusted net income	(555,093)	333,460
Diluted Earnings per Share	(1.56)	0.36
Weighted earnings per share	(1.63)	0.36
Dividends declared per share	-	0.35
Assets	60,549,350	67,541,116
Long-term debt	13,468,749	16,038,675
Shareholders' equity	10,371,231	11,449,535
Capital expenditures	147,372	80,330
Cash and marketable securities	8,033,918	7,859,280

NB: For an explanation of adjustments affecting results, see the notes of the 2018 HF Annual Report

(b) Direct Economic Benefits Generated and Distributed

HF does not receive significant financial assistance from government. We plan to participate in public-private partnerships that may involve tax incentives such as support of the government's Big Four Agenda through HFDI. This is yet to come into effect and will be prioritized in coming months.

	2018	2017
Employee compensation and benefits	1,227,077,813	1,087,999,780
Contributions to pension and social security plans	74,879,261	80,550,000
Taxes paid	513,157,762	862,008,198
Long-term debt repaid	3,522,081,000	9,075,025,000
Dividends paid to shareholders	143,365,000	186,434,000
Total charitable contributions	16,253,021	11,112,949

(c) Indirect Benefits

HF has an indirect economic impact by making it easier for small and diverse businesses to participate in the economy. We achieve this result by providing local businesses with two vital resources: procurement contracts and financial support through our lending products. In 2018, we served more than **398,704** customers and issued an average of **KShs. 3Billion** through our various lending products. We also spent approximately **KShs. 147Million** in procurement

(d) Operating Responsibly

Compliance to Applicable Laws

HF's strategy includes processes, and progress in preventing corruption and anti-competitive behavior and ensuring full compliance with law and regulation. We are not aware of any breaches of compliance in 2018 that are material to our operations or fines that are material to company assets.

2018 SUSTAINABILITY CREATION JOURNEY ABRIDGED REPORT (CONTINUED)

(e) Others

- Innovation, Research and Development through our increased used of cloud computing solutions in 2018. We also started offering incoming RTGS and EFTS enabling our customers get their funds in real time. This has improved our customer service.
- Information Security – HF Group has a number of information security policies that address privacy and protection of personal information.
- Data Protection and Privacy
- An ongoing investment in education and testing to ensure information is properly stored, accessed and shared.

Operating Responsibly in Society

The discussion concerning HF's strategy, processes, and progress in preventing corruption and anti-competitive behavior and ensuring full compliance with law and regulation is covered in other sections of this Report.

Target Actions in 2019

- **Security Training** In the coming months, employees will participate in mandatory information security training. This will take place annually.
- Increase **value chain efficiency** through an enhanced sustainability strategy and continued reporting.
- **Sustainable sourcing or procurement** from businesses that offer more sustainable options for the goods and services we need and intentionally supporting small and diverse local businesses.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for the preparation and presentation of the consolidated and separate financial statements of HF Group Plc set out on pages 74 to 169 which comprise the consolidated and separate statements of financial position as at 31 December 2018, and the consolidated and separate statement of profit or loss and other comprehensive income, consolidated and company statements of changes in equity and consolidated and separate statement of cash flows for the year then ended, and notes to the financial statements including a summary of significant accounting policies and other explanatory information.

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

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

The Directors accept responsibility for the annual and consolidated financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. The Directors are of the opinion that the financial statements give a true and fair view of the state of the financial position of the Group and the Company and of the Group and Company profit or loss.

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

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

Approval of the financial statements

The financial statements, as indicated above, were approved and authorised for issue by the Board of Directors on 28 March 2019.

Robert Kibaara: ______________	Steve Mainda: ______________
Director	Chairman
Felister Kembi: ______________	Regina Anyika: ______________
Director	Company Secretary

Date: 28 March 2019

TAARIFA KUHUSU WAJIBU WA WAKURUGENZI

Wakurugenzi wana wajibu wa kuandaa na kutoa taarifa za pamoja na za pamoja na zilizowekwa kando za matumizi ya pesa ya HF Group Plc kama ilivyofafanuliwa kutoka uk. 74 hadi 169 ambazo zinajumuisha taarifa za pamoja na za kando za hali ya kifedha kufikia Desemba 31, 2018 na taarifa ya pamoja na kando kuhusu mapato au hasara na maelezo mengine ya kina kuhusu mapato, taarifa za pamoja na kando za kampuni kuhusu mabadiliko ya umiliki wa hisa na taarifa za pamoja na kando kuhusu mtiririko wa fedha kwa kipindi cha mwaka uliomalizika na vidokezo kuhusu taarifa za matumizi ya pesa ikiwemo muhtasari wa vipengele muhimu vya sera za uhasibu na ufafanuzi wa maelezo mengine.

Wajibu wa wakurugenzi unahusu: kuhakikisha kwamba mbinu iliyotumika ya uhasibu kama ilivyofafanuliwa kupitia dokezo la 2 ni ile iliyokubalika kuandaa na kutoa taarifa ya matumizi ya pesa kwa hali ilivyo ; kuandaa na kutoa taarifa za matumizi ya pesa kwa mujibu wa viwango vya kimataifa na kwa njia ambayo inakubalika na sheria za makampuni nchini Kenya ya mwaka 2015 na kwa njia ambapo ukaguzi wa ndani ambao wakurugenzi wataona unafaa kuwezesha maandalizi ya taarifa za matumizi ya pesa zisizo hakiki iwe kwa kuhadaa au makosa.

Chini ya sheria za makampuni nchini Kenya ya mwaka 2015, wakurugenzi wanahitajika kuandaa taarifa ya matumizi ya pesa kwa kila kipindi cha matumizi ya pesa ambayo itatoa taswira (picha) halisi ya mwelekeo wa kundi na kampuni kufikia mwisho wa kipindi hicho na pia matokeo ya shughuli. Pia, inawahitaji wakurugenzi kuhakikisha kwamba kundi na kampuni zinahifadhi vyema rekodi za hesabu ambayo itafichua makadirio ya maana ya hali ya pesa ya kampuni na kundi na kampuni.

Wakurugenzi hukubali kuchukua jukumu kuhusu taarifa ya ukaguzi wa pesa ambayo imetayarishwa kwa kufuata kanuni za ukaguzi wa pesa zinazohitajika na zinazoungwa mkono na uhakiki wa maana na makadirio yanayofaa kwa kufungamana na viwango vya kimataifa na kwa njia inayolingana na sheria za makampuni nchini Kenya ya mwaka 2015. Wakurugenzi wanakubaliana kwa kauli moja kwamba, taarifa ya ukaguzi wa pesa inaonyesha hali halisi kuhusiana na maswala ya kifedha na matokeo ya shughuli za kundi na kampuni.

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

Wakurugenzi wamefanya uchunguzi wa kundi na uwezo wa kundi na kampuni kuendelea na shughuli zake na hawana tashwishi kuamini kwamba, kundi na kampuni hazitasitisha shughuli zao kwa kipindi cha miezi kumi na mbili ijayo kuanzia tarehe ya kutolewa kwa taarifa hii.

Kuidhinishwa Kwa Taarifa ya Matumizi ya Pesa

Taarifa ya matumizi ya pesa kama zilivyoonyeshwa hapo juu ziliidhinishwa na halmashauri ya Wakurugenzi mnamo tarehe 28 Machi 2019 na kutiwa sahihi kwa niaba yake na :-

Robert Kibaara: ____________________
Mkurugenzi

Steve Mainda: ____________________
Mwenyekiti

Felister Kembi: ____________________
Mkurugenzi

Regina Anyika: ____________________
Katibu wa Kampuni

Tarehe: 28 Machi 2019

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF HF GROUP PLC

Report on the audit of the financial statements

Opinion

We have audited the financial statements of HF Group Plc set out on pages 74 to 169 which comprise the Consolidated and Company statements of financial position as at 31 December 2018, the Consolidated and Company statements of profit or loss and other comprehensive income, the Consolidated and Company statements of changes in equity and the Consolidated and Company statements of cash flows for the year then ended, and notes to the financial statements including a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give a true and fair view of the consolidated and separate financial position of HF Group Plc as at 31 December 2018, and of its consolidated and separate financial performance and consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) and in the manner required by the Kenyan Companies Act, 2015.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *'Auditors' Responsibilities for the Audit of the Financial Statements'* section of our report. We are independent of the Group and Company in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (IESBA Code)* together with the ethical requirements that are relevant to our audit of the financial statements in Kenya and, we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

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

Impairment of loan and advances to customers	
See accounting policy note 3(i)(v) - Significant accounting policies and disclosure Note 18 – Loans and advances to customers.	
The key audit matter	**How the matter was addressed**
On 1 January 2018, the Group adopted IFRS 9 Financial Instruments, resulting in impairment charges being recognised when losses are expected rather than when they are incurred. Impairment of loans and advances to customers is considered a key audit matter because the directors make complex and subjective judgments over both timing of recognition of impairment and the estimation of the size of any such impairment.	Based on our risk assessment and industry knowledge, we have examined the impairment charges for loans to customers and evaluated the methodology applied as well as the assumptions made according to the description of the key audit matter. *Our audit procedures in this area included, among others:*

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF HF GROUP PLC (CONTINUED)

Report on the audit of the financial statements (continued)

Key audit matters - continued

Impairment of loan and advances to customers (Continued)	
See accounting policy note 3(i)(v) - Significant accounting policies and disclosure Note 18 – Loans and advances to customers.	
The key audit matter	**How the matter was addressed**
Management has disclosed information regarding the transitional effect of this new and complex standard in accounting policy notes 3(i), 4(a) and 4(b). The key areas where we identified greater levels of management judgement and therefore increased levels of audit focus in the Group's implementation of IFRS 9 are: *Economic scenarios* IFRS 9 requires Expected Credit Loss (ECL) to be measured on a forward-looking basis reflecting a range of future economic conditions. Significant management judgement is applied in determining the economic scenarios used and the probability weightings applied to them and the associated impact on ECL. *Significant Increase in Credit Risk ('SICR')* The criteria selected to identify a significant increase in credit risk is a key area of judgement within the Group's ECL calculation as these criteria determine whether a 12-month or lifetime expected credit loss is assessed. *Complex ECL models* Inherently, judgemental modelling is used to estimate ECLs which involves determining Probabilities of Default ('PD'), Loss Given Default ('LGD'), and Exposures at Default ('EAD') and ultimately the Expected Credit Loss (ECL). The PD models used in the different loan portfolios are the key drivers of the Group's ECL results and are therefore most significant judgemental aspect of the Group's ECL modelling approach. *Qualitative adjustments (management overlays)* Adjustments to the model-driven ECL results are raised by management to address known impairment model limitations or emerging risks and trends in underlying portfolios. Such adjustments are inherently uncertain and significant management judgement is involved in estimating these amounts.	— Involving our own IFRS 9 and data and analytics specialists in evaluating the appropriateness of the Group's IFRS 9 impairment methodologies and independently assessing the accuracy of probability of default, loss given default and exposure at default computations and assumptions. — Involving our own financial risk management specialists in: assessing the appropriateness of the Group's methodology for determining the economic scenarios used and the probability weightings applied to them; assessing the economic variables used which included agreeing them to independent external sources; and assessing the overall reasonableness of the economic forecasts applied by the Group; and reviewing management considerations of the ECL impact of economic uncertainty in the market. — Selecting a sample of facilities from the Group's loan book and performing tests to establish whether significant facilities are correctly staged/classified and valued based on IFRS; — Performing credit assessment on various categories of loans to ascertain the reasonableness of the forecast of recoverable cash flows, realisation of collateral, and other sources of repayment for defaulted loans. We compared key assumptions to progress against business plans and our own understanding of the relevant industries and business environments; — Testing of a sample of key data inputs and assumptions impacting ECL calculations to assess the reasonableness of economic forecasts and PD assumptions applied; — Evaluating the appropriateness of the Group's IFRS 9 methodologies including the SICR criteria used;.

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF HF GROUP PLC (CONTINUED)

Report on the audit of the financial statements (continued)

Key audit matters - continued

Impairment of loan and advances to customers (Continued)	
See accounting policy note 3(i)(v) - Significant accounting policies and disclosure Note 18 – Loans and advances to customers.	
The key audit matter	**How the matter was addressed**
Disclosure quality The disclosures regarding the Group's application of IFRS 9 are key to understanding the change from IAS 39 as well as explaining the key judgements and material inputs to the IFRS 9 ECL results.	— Testing the impairment calculations to check if the correct parameters – Probability of Default (PDs, Loss Given Default (LGDs), and Exposure at Default (EADs) were determined by considering local economic/portfolio factors; and — Assessing whether the disclosures appropriately disclose the key judgements and assumptions used in determining the expected credit losses
Provisions and contingent liabilities in respect of litigations	
See accounting policy note 3 (l) – Significant accounting policies and disclosure note 36 - Contingent liabilities.	
The key audit matter	**How the matter was addressed**
The Group and Company are subject to claims, which could have an impact on the results if the potential exposures were to materialise. In the normal course of business, potential exposures may arise from general legal proceedings, product liability, guarantees, and regulator investigations/reviews. Whether there is a liability is inherently uncertain, the amounts involved are potentially significant and the application of accounting standards to determine the amount, if any, to be provided as a liability, is inherently subjective. The directors apply judgment when considering whether, and how much, to provide for the potential exposure of each litigation and/or claim. We focused on this area given the complexity and judgment necessary to determine whether to provide for, disclose or not disclose certain exposures.	Our audit procedures in this area included, among others: — Performing control assessment of the processes and controls over claims and oversight of litigations by the Directors. We held discussions with the in-house legal counsel, including after the year end, to discuss the nature of all significant on-going claims and legal cases, and to validate the latest status and accounting and disclosure implications; — Obtaining formal legal confirmations from external legal counsel for significant litigation matters to ensure completeness of provisions and disclosures, where required, and also analysing correspondence with regulators; and — Assessing the legal opinion from the external lawyers to challenge the basis used for the provisions recorded or disclosures made by the Directors. Where provisions were not required, considering the adequacy and completeness of the Group's and Company's disclosures made in relation to contingent liabilities.
Information Technology (IT) systems and control	
The Group's financial accounting and reporting processes are highly dependent on the automated controls over the information systems such that there exists a risk that gaps in the IT control environment could result in the financial accounting and reporting records being materially misstated. For example interfaces between the operating systems and financial reporting systems, or automated controls that prevent or detect inaccurate or incomplete transfers of financial information. If these systems or controls fail, a significant risk of error in reported financial information can arise from the failure to transfer data appropriately between systems or inappropriate changes being made to financial data or systems. Our audit effort focused on key systems used by the Group. This is an area requiring particular audit attention in our audit due to the complexity of the IT infrastructure.	Our audit procedures in this area included, among others: — Evaluating the design and testing the operating effectiveness of the controls over the continued integrity of the IT systems that are relevant to financial reporting. — Examining the framework of governance over the Group's IT organisation and the controls over access to programs and data, program changes, IT operations and program development; — Where necessary, carrying out direct tests of certain aspects of the security of the Group's IT systems including logical access management and segregation of duties; and — Testing the design and operating effectiveness of automated controls critical to financial reporting (application controls). For any identified deficiencies, we tested the design and effectiveness of compensating controls and, where necessary, extended the scope of our substantive audit procedures.

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF HF GROUP PLC (CONTINUED)

Report on the audit of the financial statements (continued)

Other information

The directors are responsible for the other information. The other information comprises the information included in the Annual Report and Financial Statements, but does not include the financial statements and our auditors' report there on.

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

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

Directors' responsibilities for the financial statements

As stated on page 66, the directors are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards, and in the manner required by the Kenyan Companies Act, 2015 and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

The directors are responsible for overseeing the Group's and Company's financial reporting process.

Auditors' responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF HF GROUP PLC (CONTINUED)

Auditors' responsibilities for the audit of the financial statements (continued)

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's and Company's internal control;
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors;
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the group and / or the company to cease to continue as a going concern;
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation; and

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

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

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

Report on other legal and regulatory requirements

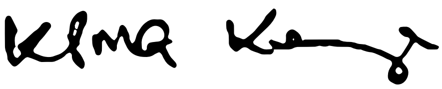
As required by the Kenyan Companies Act, 2015 we report to you based on our audit, that:

(i) In our opinion, the information in the report of the directors on pages 41 and 42 is consistent with the financial statements;

(ii) In our opinion, the auditable part of the directors' remuneration report on pages 45 to 47 has been properly prepared in accordance with the Kenyan Companies Act, 2015; and

(iii) Our opinion is unqualified.

The Signing Partner responsible for the audit resulting in this independent auditors' report is FCPA Eric Aholi – P/1471.



KPMG Kenya
Certified Public Accountants
P.O. Box 40612 – 00100, Nairobi

Date: 28 March 2019

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HF Group PLC is regulated as a non-operating company by the Central Bank of Kenya.

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018 KShs'000	2017 KShs'000
Interest income	7	6,045,521	7,132,626
Interest expense	7	(3,779,848)	(4,156,258)
Net interest income		**2,265,673**	**2,976,368**
Impairment losses financial instruments	18(b)	(375,908)	(576,203)
Net interest income after impairment losses on financial instruments		**1,889,765**	**2,400,165**
Non-interest income	8	1,319,057	1,346,426
Non-interest expenses	9	(3,860,507)	(3,412,196)
Share of profit in joint ventures	19(b)	8,941	(22,771)
(Loss)/profit before tax	10	**(642,744)**	**311,624**
Income tax expense	11	44,526	(185,408)
Net (loss)/profit after tax for the year		(598,218)	126,216
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Revaluation surplus	33(d)	860	189,032
Related tax		-	(9,452)
		860	179,580
Movement in fair value reserve on FVOCI investments	33(f)	60,379	-
Movement in fair value reserve on available for sale investments	33(f)	-	39,520
Related tax	33(f)	(18,114)	(11,856)
		42,265	27,664
Total comprehensive income for the year		**(555,093)**	**333,460**
Annualised basic and diluted earnings per share – KShs	12	**(1.56)**	**0 .36**
Weighted earnings per share	12	**(1.63)**	**0.36**
Dividends per share – KShs	13(a)	**-**	**0.35**
Number of shares	33(b)	**384,614**	**349,537**
Weighted number of shares	12	**367,135**	**349,537**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

COMPANY STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2018

		2018	2017
	Note	**KShs'000**	**KShs'000**
Interest income	7	605	1,448
Interest expense		-	-
Net interest income		**605**	**1,448**
Non-interest income	8	387,934	421,282
Non-interest expenses	9	(358,941)	(238,629)
Profit before tax	10	**29,598**	**184,101**
Income tax expense	11(a)	11,904	(412)
Profit after tax		**41,502**	**183,689**
Other comprehensive income		-	-
Total comprehensive income		**41,502**	**183,689**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2018

	Note	2018 KShs'000	2017 KShs'000
ASSETS			
Cash and balances with banks	15	2,917,083	4,079,347
Placements with other banks	16	1,904,695	1,492,637
Investment in government securities	17	3,212,140	2,287,296
Loans and advances to banks	18(a)	253,404	270,953
Loans and advances to customers (Net)	18(a)	43,186,287	49,368,686
Investment in joint ventures	19(b)	1,690,210	1,713,985
Other assets	20	411,411	1,487,808
Investment Property	30	-	748,549
Housing development projects	21	2,537,972	2,414,469
Property and equipment	22(a)	2,078,978	1,517,380
Prepaid operating lease rentals	23	43,284	44,108
Intangible assets	24	1,007,553	1,072,387
Tax recoverable	11(b)	311,739	204,012
Deferred tax asset	25(a)	994,594	839,499
TOTAL ASSETS		**60,549,350**	**67,541,116**
LIABILITIES			
Deposits from customers	27	34,720,824	36,660,581
Deposits from banks	28	578,216	83,692
Other liabilities	29	1,382,272	3,259,572
Tax payable	11(b)	3	3
Dividends – payable	13(b)	28,055	49,058
Loans from financial institutions	31(a)	8,469,153	11,541,643
Borrowings	31(b)	1,947,785	1,449,663
Corporate bond	32	3,051,811	3,047,369
		50,178,119	**56,091,581**
SHAREHOLDERS' EQUITY			
Share capital	33(b)	1,923,071	1,747,683
Share premium	33(c)	4,343,512	4,342,912
Statutory credit risk reserve	33(e)	1,885,489	640,800
Other reserves		875,942	832,817
Retained earnings		1,292,467	3,834,573
Shareholders' income notes and loans	34	50,750	50,750
		10,371,231	**11,449,535**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**60,549,350**	**67,541,116**

The financial statements set on pages 74 to 169 were approved and authorised for issue by the Board of Directors on 28 March 2019 and signed on its behalf by:

Robert Kibaara:__________________
Director

Felister Kembi:__________________
Director

Steve Mainda: __________________
Chairman

Regina Anyika:__________________
Company Secretary

The notes set out on pages 84 to 169 form an integral part of these financial statements.

COMPANY STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2018

	Note	2018 KShs'000	2017 KShs'000
ASSETS			
Cash and balances with banks	15	34,167	28,384
Investment in subsidiaries	19(a)	9,958,782	9,958,782
Other assets	20	97,113	54,542
Property and equipment	22(b)	695	572
Tax recoverable	11(b)	25,133	13,585
Deferred tax asset	25(b)	15,854	22
TOTAL ASSETS		**10,131,744**	**10,055,887**
LIABILITIES			
Other liabilities	29	251,422	111,156
Dividends - payable	13(b)	28,055	49,058
		279,477	**160,214**
SHAREHOLDERS' EQUITY			
Share capital	33(b)	1,923,071	1,747,683
Share Premium	33(c)	4,343,512	4,343,912
Retained Earnings		3,585,684	3,682,719
Proposed Dividends		-	122,359
		9,852,267	**9,895,673**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**10,131,744**	**10,055,887**

The financial statements set on pages 74 to 169 were approved and authorised for issue by the Board of Directors on 28 March 2019 and signed on its behalf by:

Robert Kibaara:______________________
Director

Steve Mainda:______________________
Chairman

Felister Kembi:______________________
Director

Regina Anyika:______________________
Company Secretary

The notes set out on pages 84 to 169 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018 KShs'000	2017 KShs'000
Net cash flows from operating activities	35(a)	**2,204,386**	**5,217,834**
INVESTING ACTIVITIES			
Purchase of property and equipment	22	(11,975)	(38,170)
Investment in joint ventures	19(b)	1,210	(456,646)
Proceeds from sale of equipments	22	389	-
Additions to intangible assets	24	(135,397)	(42,160)
Net cash used in investing activities		**(145,773)**	**(536,976)**
FINANCING ACTIVITIES			
Receipts of borrowed funds	31(c)	952,156	5,377,085
Payments of borrowed funds	31(c) & 32	(3,522,081)	(9,075,025)
Share ownership plan receipts	26	1,200	1,550
Dividend paid	13(b)	(143,365)	(186,434)
Net cash used in financing activities		**(2,712,090)**	**(3,882,824)**
Net (decrease)/increase in cash and cash equivalents	35(b)	**(653,477)**	**798,034**
Cash and cash equivalents as at 1 January		3,662,849	2,864,815
Cash and cash equivalents as at 31 December		**3,009,372**	**3,662,849**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

COMPANY STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018 KShs' 000	2017 KShs' 000
Net cash flows from operating activities	35(c)	**148,213**	**145,816**
INVESTING ACTIVITIES			
Purchase of equipment	22(b)	(265)	(380)
Net cash used in investing activities		**(265)**	**(380)**
FINANCING ACTIVITIES			
Employee share ownership	26	1,200	1,550
Dividend paid	13(b)	(143,365)	(186,434)
Net cash used in financing activities		**(142,165)**	**(184,884)**
Increase/(decrease) in cash and cash equivalents	35(d)	**5,783**	**(39,448)**
Cash and cash equivalent at 1 January		28,384	67,832
Change in the year		5,783	(39,448)
Cash and cash equivalent at 31 December	35(d)	**34,167**	**28,384**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018

	Share capital	Revaluation reserve	Share premium	Proposed dividends	Statutory credit risk Reserve	Retained earnings	Fair value reserve	Total
	Kshs '000	Kshs '000	Kshs '000	Kshs'000	Kshs '000	Kshs '000	Kshs '000	Kshs '000
31 December 2017	**1,747,683**	**881,043**	**4,342,912**	**122,359**	**640,800**	**3,712,214**	**(48,226)**	**11,398,785**
Adjustments on initial application of IFRS 9 (note 4b)	-	-	-	-	-	(360,061)	-	**(360,061)**
Related tax (note 25)	-	-	-	-	-	108,018	-	**108,018**
Transfer from statutory reserve	-	-	-	-	(283,976)	283,976	-	**-**
Adjustments on initial application of IFRS 15 (note 3(o)(i)	-	-	-	-	-	(200,791)	-	**(200,791)**
Related tax (note 11(b))	-	-	-	-	-	50,785	-	**50,785**
Restated balance at 1 January 2018	**1,747,683**	**881,043**	**4,342,912**	**122,359**	**356,824**	**3,594,141**	**(48,226)**	**10,996,736**
Total comprehensive income								
Net profit after tax	-	-	-	-	-	(598,218)	-	**(598,218)**
Other comprehensive income								
Revaluation Surplus	-	860	-	-	-	-	-	**860**
Net gain on investments in financial instruments	-	-	-	-	-	-	60,379	**60,379**
Related tax	-	-	-	-	-	-	(18,114)	**(18,114)**
Transfer to statutory reserve	-	-	-	-	1,528,665	(1,528,665)	-	**-**
Total other comprehensive Income	**-**	**860**	**-**	**-**	**1,528,665**	**(1,528,665)**	**42,265**	**43,125**
Total comprehensive Income	**-**	**860**	**-**	**-**	**1,528,665**	**(2,126,883)**	**42,265**	**(555,093)**
Transactions with owners, recorded directly in equity								
Employee Share Ownership Plan	600	-	600	-	-	-	-	**1,200**
Dividend paid – 2017	-	-	-	(122,359)	**-**	(3)	-	**(122,362)**
Bonus Share issue	174,788	-	-	-	-	(174,788)	-	**-**
Total transactions with owners for the year	**175,388**	**-**	**600**	**(122,359)**	**-**	**(174,791)**	**-**	**(121,162)**
At 31 December 2018	**1,923,071**	**881,903**	**4,343,512**	**-**	**1,885,489**	**1,292,467**	**(5,961)**	**10,320,481**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

	Share capital	Revaluation reserve	Share premium	Proposed dividends	Statutory credit risk reserve	Retained earnings	Fair Value reserve	Total
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
At 1 January 2017	1,746,908	701,463	4,342,137	174,691	453,487	3,895,716	(75,890)	11,238,512
Total comprehensive income for the year								
Net profit after tax	-	-	-	-	-	126,216	-	126,216
Other comprehensive income								
Revaluation surplus	-	189,032	-	-	-	-	-	189,032
Change in fair value of available-for-sale investment	-	-	-	-	-	-	39,520	39,520
Related tax	-	(9,452)	-	-	-	-	(11,856)	(21,308)
Transfer to statutory credit risk reserve	-	-	-	-	187,313		-	-
Total other comprehensive Income	**-**	**179,580**	**-**	**-**	**183,313**	**(187,313)**	**27,664**	**207,244**
Total comprehensive Income	**-**	**179,580**	**-**	**-**	**187,313**	**(61,097)**	**27,664**	**333,460**
Transactions with owners, recorded directly in equity								
Employee Share Ownership Plan	775	-	775	-	-	-	-	1,550
Dividend paid – 2016	-	-	-	(174,691)	-	(46)	-	(174,737)
Interim dividend paid - 2017								
Proposed dividends	-	-	-	122,359	-	(122,359)	-	-
Total transactions with owners for the year	**775**	**-**	**775**	**(52,332)**	**-**	**(122,405)**	**-**	**(173,187)**
Balance as at 31 December 2017	**1,747,683**	**881,043**	**4,342,912**	**122,359**	**640,800**	**3,712,214**	**(48,226)**	**11,398,785**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018

	Share capital	Share premium	Proposed dividends	Retained earnings	Total
	Kshs '000	Kshs '000	Kshs '000	Kshs '000	Kshs '000
At 31 December 2017	**1,747,683**	**4,342,912**	**122,359**	**3,682,720**	**9,895,674**
Adjustments on initial application of IFRS 9	-	-	-	(12,847)	**(12,847)**
Related Tax	-	-	-	3,854	**3,854**
Prior year adjustment of fair value reserves	-	-	-	45,246	**45,246**
Restated balance at 1 January 2018	**1,747,683**	**4,342,912**	**122,359**	**3,718,973**	**9,931,927**
Total comprehensive income					
Net profit after tax	-	-	-	41,502	**41,502**
Total comprehensive Income	-	**-**	-	**41,502**	**41,502**
Transactions with owners, recorded directly in equity					
Employee Share Ownership Plan	600	600	-	-	**1,200**
Dividend paid – 2017	-	-	(122,359)	(3)	**(122,362)**
Bonus Share issue	174,788	-	-	(174,788)	**-**
Total transactions with owners for the year	**175,388**	**600**	**(122,359)**	**(174,791)**	**(121,162)**
At 31 December 2018	**1,923,071**	**4,343,512**	**-**	**3,585,684**	**9,852,267**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

	Share capital KShs'000	Share premium KShs'000	Proposed dividends KShs'000	Retained profits KShs'000	Total KShs'000
At 1 January 2017	**1,746,908**	**4,342,137**	**174,691**	**3,621,432**	**9,885,168**
Net profit after tax	-	-	-	183,689	183,689
Other comprehensive income	**-**	**-**	**-**	**183,689**	**183,689**
Total comprehensive income for the year	**-**	**-**	**-**	**183,689**	**183,689**
Transactions with owners, recorded directly in equity					
Employee Share Ownership Plan	775	775	-	-	1,550
Dividend paid – 2016	-	-	(174,691)	(42)	(174,733)
Proposed dividends	-	-	122,359	(122,359)	-
Total transactions with owners for the year	**775**	**775**	**(52,332)**	**(122,401)**	**(173,183)**
Balance as at 31 December 2017	**1,747,683**	**4,342,912**	**122,359**	**3,682,720**	**9,895,674**

The notes set out on pages 84 to 169 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018

1. GENERAL INFORMATION

HF Group PLC is incorporated as a limited company in Kenya under the Kenyan Companies Act, 2015 and is domiciled in Kenya. The address of the company's registered office is shown on Page 4. The consolidated financial statements comprise of the Company and its subsidiaries (together referred as the "Group" or "Consolidated" and individually reffered to as "Group entities").

The Group is primarily involved in mortgage lending, provision of corporate and retail banking solutions, property development, bancassurance services, and social investment.

2. BASIS OF PREPARATION

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

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) and the Kenyan Companies Act, 2015.

Details of the Group's significant accounting policies are included in Notes 3.

This is the first set of the Group's annual financial statements in which IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers have been applied. Resultant changes to significant accounting policies are described in Note 3.

Due to the transition method chosen by the Group in applying these standards, comparative information throughout these financial statements has not generally been restated to reflect the requirements of the new standards.

The effect of initially applying these standards is mainly attributed to the following:

– an increase in impairment losses recognised on financial assets (Note 4 (a)).
– additional disclosures related to IFRS 9 (see Note 4 (a) and (b)); and
– additional disclosures related to IFRS 15 (see Note 3 (o)).
– delayed recognition of revenue from sale of houses (see note 3 (o))

Except for the changes above, the Group has consistently applied the accounting policies as set out in Note 3 to all periods presented in these financial statements.

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

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

2. BASIS OF PREPARATION (Continued)

(b) Basis of measurement

The measurement basis used is the historical cost basis except where otherwise stated in the accounting policies below.

For those assets and liabilities measured at fair value, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When measuring the fair value of an asset or a liability, the Group uses market observable data as far as possible. If the fair value of an asset or a liability is not directly observable, it is estimated by the Group using valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs (e.g. by use of the market comparable approach that reflects recent transaction prices for similar items or discounted cash flow analysis). Inputs used are consistent with the characteristics of the asset/liability that market participants would take into account.

Fair values are categorised into three levels of fair value hierarchy based on the degree to which the inputs to the measurements are observable and the significance of the inputs to the fair value measurement in its entirety:

Level 1 – fair value measurements are derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 – fair value measurements are derived from inputs other than quoted prices used in Level 1that are observable for the assets or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 – fair values measurements are derived from valuation techniques that include inputs for assets or liabilities that are not based on observable market data (unobservable inputs).

Transfers between levels of the fair value hierarchy are recognised by the Group at the end of the reporting period during which the change occurred.

(c) Functional and presentation currency

These financial statements are presented in Kenya Shillings (KShs),which is the Group'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. Except as otherwise indicated, financial information presented in Kenya Shillings has been rounded to the nearest thousand (KShs'000).

(d) Use of estimates and judgements

The preparation of financial statements in comformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, incomes and expenses. Actual results may ultimately differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

In particular, information about significant areas of estimation and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements is described in Note 5.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented on these financial statements:

(a) Revenue recognition

(i) Interest

Policy applicable before 1 January 2018

Effective interest rate

Interest income and expense were recognised in profit or loss using the effective interest method. The effective interest rate was the rate that exactly discounted the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimated future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate included transaction costs and fees and points paid or received that were an integral part of the effective interest rate. Transaction costs included incremental costs that were directly attributable to the acquisition or issue of a financial asset or financial liability.

Presentation

Interest income calculated using the effective interest method presented in the statement of profit or loss and OCI included:

- interest on financial assets and financial liabilities measured at amortised cost;
- interest on debt instruments measured at FVOCI;
- the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period as the hedged cash flows affect interest income/expense; and
- the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

Other interest income presented in the statement of profit or loss and OCI included interest income on finance leases.

—Interest expense presented in the statement of profit or loss and OCI included:

- financial liabilities measured at amortised cost; and
- the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period as the hedged cash flows affect interest income/expense.

Interest income and expense on all trading assets and liabilities were considered to be incidental to the Group's trading operations and were presented together with all other changes in the fair value of trading assets and liabilities in net trading income.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(a) Revenue recognition (continued)

(i) Interest - continued

Policy applicable from 1 January 2018 - continued

Interest income and expense are recognised in profit or loss using the effective interest method.

The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

— the gross carrying amount of the financial asset; or
— the amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Group estimates future cash flows considering all contractual terms of the financial instrument, but not ECL. For purchased or originated credit impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.

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

Amortised cost and gross carrying amount

The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance (or impairment allowance before 1 January 2018). The 'gross carrying amount of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest. The effective interest rate is also revised for fair value hedge adjustments at the date amortisation of the hedge adjustment begins.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(a) Revenue recognition (continued)

(i) Interest - continued

Policy applicable from 1 January 2018 - continued

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

Presentation

Interest income calculated using the effective interest method presented in the statement of profit or loss and OCI includes:

— interest on financial assets and financial liabilities measured at amortised cost;
— interest on debt instruments measured at FVOCI;
— the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period as the hedged cash flows affect interest income/expense; and
— the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

Other interest income presented in the statement of profit or loss and OCI includes interest income on finance leases.

Interest expense presented in the statement of profit or loss and OCI includes:

— financial liabilities measured at amortised cost; and
— the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period as the hedged cash flows affect interest income/expense.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the Group's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income.

Interest income and expense on other financial assets and financial liabilities at FVTPL are presented in net income from other financial instruments at FVTPL

(ii) Non interest income

Fees and commission income

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

Other fees and commission income, including account servicing fees, are recognised as the related services are performed. Other fees and commission expenses relate mainly to transaction and services fees, which are expensed as the services are received.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) Property and equipment

(i) Recognition and measurement

All categories of property and equipment are initially recorded at cost. Property and equipment is subsequently shown at a revalued amount, being its fair value at the date of revaluation less any subsequent accumulated depreciation and impairment losses. Valuations are performed, every three years, by external independent valuers. Purchased software that is integral to the functioning of related equipment is capitalized as part of that equipment. Increases in the carrying amount arising on revaluation are credited to other comprehensive income. Decreases that offset previous increases of the same asset are charged against the revaluation surplus; all other decreases are charged to the profit or loss.

The cost of replacing a component of an item of property and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The carrying amount of the replaced item is derecognized. The cost of day to day servicing of property and equipment is recognized in the profit and loss.

(ii) Depreciation

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 shorter of 50 years and the remaining period of the lease. Buildings on freehold land are depreciated over fifty years.

Depreciation method, useful lives and residual values are reassessed at the reporting date.

(iii) Disposal of property and equipment

Gains and losses on disposal of property and equipment are determined by reference to the carrying amount and are recognised in profit or loss in the period in which they arise.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(d) Intangible assets

Where computer software is not an integral part of the related computer hardware it is recognised as an intangible asset. The software is stated on the statement of financial position at costs less accumulated amortisation and impairment losses. Subsequent expenditure on software assets is capitalised only when it increases the future economic benefit embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Software costs are amortised over the estimated useful life, currently estimated at five (5) to (8) years, on a straight line basis from the date the software is available for use.

(e) Prepaid operating lease rental

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 post-paid) are charged to profit or loss on a straight-line basis over the period of the lease.

(f) Employee benefits

(i) Employee Retirement Benefits Plan

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

The employees and the Group also contribute to the National Social Security Fund, a national retirement benefit scheme. Contributions are determined by the local statute and the Group's contributions are charged to profit or loss in the period to which they relate. The Group has no further obligation once the contributions have been paid.

(ii) Accrued leave

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

(iii) Termination benefits

Termination benefits are recognised as an expense when the Group is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised if the Group has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(f) Employee benefits (continued)

(iv) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(v) Provisions for liability

Provisions for restructuring costs and legal claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

(g) Taxation

Tax on the operating results for the period comprises current tax and change in deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that they relate to items recognised directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using tax rates enacted or substantively enacted at the reporting date, and any adjustments to tax payable in respect of previous years. Current tax is provided on the results in the period as shown in the financial statements adjusted in accordance with tax legislation.

Deferred tax is recognized in respect of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss; and
- taxable temporary differences arising on the initial recognition of goodwill.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(g) Taxation (continued)

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised for unused tax losses and deductible temporary differences to the extent that it is probable that future taxable profit will be available against which the tax asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Deferred tax is calculated on the basis of the tax rates enacted at the reporting date.

(h) Cash and cash equivalents

Cash and cash equivalents include cash in hand, bank deposits held at call, unrestricted balances held with the central bank and highly liquid financial assets with original maturities of three months or less from the date of acquisition that are subject to an insignificant risk of changes in their fair value and are used by the Group in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

(i) Financial assets and liabilities

Policy applicable from 1 January 2018

(i) Recognition

The Group initially recognises loans and advances to customers, deposits and debt securities on the date at which they are originated. All other financial assets and liabilities (including assets designated at fair value through profit and loss) are initially recognised on the trade date at which the Group becomes a party to the contractual provision of the instrument.

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

Subsequent to initial recognition, financial liabilities (deposits and debt securities) are measured at their amortized cost using the effective interest method except where the Group designates liabilities at fair value through profit and loss.

(ii) Classification

Financial assets

The Group classifies its financial assets on initial recognition into three principal classification categories based on the cash flow characteristics of the asset and the business model assessment:

— measured at Amortised Cost;

— Fair Value through Other Comprehensive Income (FVOCI); and

— Fair Value through Profit or Loss (FVTPL)

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED))

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(ii) Classification (continued)

The previous categories of Held to Maturity, Loans and Receivables and Available for Sale under IAS 39 have been replaced.

Financial liabilities

IFRS 9 largely retains the existing requirements in IAS 39 for the classification and measurement of financial liabilities. However, although under IAS 39 fair value changes of liabilities designated under the fair value option were recognised in profit and loss, under IFRS 9 fair value changes are generally presented as follows:

— the amount of change in fair value that is attributable to changes in credit risk of the liability is presented in OCI and;
— the remaining amount of change in fair value is presented in profit or loss.

The Group classifies all financial liabilities as subsequently measured at amortised cost.

Customer deposits, balances due to banking institutions and other liabilities are classified at amortised cost.

Amortised cost

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:
— it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
— its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

The Group recognises cash and balances with Central Bank, placements with other banks, investments in government securities, loans and advances to customers and other assets at amortised cost.

Fair Value through Other Comprehensive Income (FVOCI) – Debt

A financial asset which is a debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:
— it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
— its contractual terms give rise on specified dates to cash flows that are solely payments of principal and Interest (SPPI) on the principal amount outstanding.

The Group has no financial debts classified at FVOCI.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(ii) Classification (continued)

Fair Value through Other Comprehensive Income (FVOCI) – Equity

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by investment basis. The Group currently does not have any equity investments.

Fair Value through Profit or Loss (FVTPL)

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. In addition, on initial recognition the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

The Group does not have financial assets classified at FVTPL.

Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of IFRS 9 are not separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

Assessment of whether contractual cash flows are solely payments of principal and Interest (SSPI)

To determine whether a financial asset should be classified as measured at amortised cost, FVOCI or FVTPL, an entity assesses whether the cash flows from the financial asset represent, on specified dates, solely payments of principal and interest on the principal amount outstanding i.e. the SPPI criterion. A financial asset that does not meet the SPPI criterion is always measured at FVTPL, unless it is an equity instrument for which an entity applies the FVOCI election.

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. The definition of principal reflects the economics of the financial asset from the perspective of the current holder. This means that an entity assesses the asset's contractual cash flow characteristics by comparing the contractual cash flows to the amount that it actually invested.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(ii) Classification (continued)

Assessment of whether contractual cash flows are solely payments of principal and Interest (SSPI) - continued

'Interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Group considers the contractual terms of the instrument. This included assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Group considers:

— contingent events that would change the amount and timing of cash flows;
— leverage features;
— prepayment and extension terms;
— terms that limit the Group's claim to cash flows from specified assets – e.g. non-recourse asset arrangements; and
— features that modify consideration for the time value of money – e.g. periodic reset of interest rates.

Contractual features that introduce exposure to risks or volatility in the contractual cash flows that is unrelated to a basic lending arrangement, such as exposure to changes in equity prices or commodity prices, give rise to contractual cash flows that do not meet the SPPI criterion.

Non-recourse loans

In some cases, loans made by the Group that are secured by collateral of the borrower limit the Group's claim to cash flows of the underlying collateral (non-recourse loans). The group applies judgment in assessing whether the non-recourse loans meet the SPPI criterion. The Group typically considers the following information when making this judgement:

— whether the contractual arrangement specifically defines the amounts and dates of the cash payments of the loan;
— the fair value of the collateral relative to the amount of the secured financial asset;
— the ability and willingness of the borrower to make contractual payments, notwithstanding a decline in the value of collateral;
— whether the borrower is an individual or a substantive operating entity or is a special-purpose entity;
— the Group's risk of loss on the asset relative to a full-recourse loan;
— the extent to which the collateral represents all or a substantial portion of the borrower's assets; and
— whether the Group will benefit from any upside from the underlying assets.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(ii) Classification (continued)

Assessment of whether contractual cash flows are solely payments of principal and Interest (SSPI) - continued

The Group also provides floating interest rate loans. The Group has determined that the contractual cash flows of these loans and advances are SPPI because the interest is not leveraged and though may vary will still represent consideration for time value of money or other basic lending.

De minimis

A contractual cash flow characteristic does not affect the classification of a financial asset if it could have only a de minimis effect on the financial asset's contractual cash flows.

To make this determination, the Group considers the possible effect of the contractual cash flow characteristic in each reporting period and cumulatively over the life of the financial asset.

Business model assessment

The Group makes an assessment of the objective of the business model in which a financial asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

— the stated policies and objectives for the portfolio and the operation of those policies in practice, including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
— how the performance of the portfolio is evaluated and reported to the Group's management;
— the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
— how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
— the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(iii) Derecognition

The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

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

(iv) Offsetting

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

(v) Measurement of expected credit loss

FRS 9 replaced the previous 'incurred loss' model in IAS 39 with a forward-looking 'expected credit loss' model.

The Group recognises loss allowances for ECL on the following financial instrument Group s that are not measured at FVTPL:

- financial assets that are debt instruments – this applies to the Group's loans and advances to customers, cash and balances with Central Bank, investments in government securities, placements with other banking institutions and other assets; and
- Loan commitments and financial guarantee contracts issued (previously, impairment was measured under IAS 37 Provisions, Contingent Liabilities and Contingent Assets) - this applies to the Group's off balance sheet exposures where credit intervention is not required for the counterparty to access the credit facility.

No impairment loss is recognised on equity investments.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(v) Measurement of expected credit loss - continued

The Group recognises loss allowance at an amount equal to either 12-month ECLs or lifetime ECLs. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument, whereas 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date (or a shorter period if the expected life of a financial instrument is less than 12 months), weighted by the probability of that default occurring.

The Group recognises loss allowances at an amount equal to lifetime ECLs, except in the cases where credit risk has not increased significantly since initial recognition. Loss allowances for trade and lease receivables will always be measured at an amount equal to lifetime ECLs applying the simplified approach.

The impairment requirements of IFRS 9 are complex and require management judgements, estimates and assumptions, particularly in the following areas, which are discussed in detail below and in note 4(a):

— assessing whether the credit risk of an instrument has increased significantly since initial recognition; and

— incorporating forward-looking information into the measurement of ECLs.

ECLs are a probability-weighted estimate of credit losses and will be measured as follows:

— financial assets that are not credit-impaired at the reporting date: the present value of all cash shortfalls i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive;

— financial assets that are credit-impaired at the reporting date: the difference between the gross carrying amount and the present value of estimated future cash flows;

— undrawn loan commitments: the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and

— financial guarantee contracts: the present value of the expected payments to reimburse the holder less any amounts that the Group expects to recover.

An asset is credit-impaired if one or more events have occurred that have a detrimental impact on the estimated future cash flows of the asset. The following are examples of such events:

—significant financial difficulty of the issuer or the borrower;

— a breach of contract - e.g. a default or past-due event;

— a lender having granted a concession to the borrower - for economic or contractual reasons relating to the borrower's financial difficulty - that the lender would not otherwise consider;

— it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;

— the disappearance of an active market for that financial asset because of financial difficulties; or

— the purchase of a financial asset at a deep discount that reflects the incurred credit losses.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

(vi) Significant increase of credit risk

The Group continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12 month ECL or LTECL, the Group assesses whether there has been a significant increase in credit risk since initial recognition. The Group considers an exposure to have significantly increased in credit risk when there is a relative change in probability of default since origination, and certain other criteria, such as 30-day past due and watchlist status. There is a rebuttable presumption that the credit risk on a financial asset has increased significantly since initial recognition when contractual payments are more than 30 days past due.

The Group also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming forborne. In certain cases, the Group may also consider that some events are a significant increase in credit risk as opposed to a default. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

When estimating ECLs on a collective basis for a group of similar assets, the Group applies the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

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

The Group segments its retail lending products into portfolios, based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and involves a wider set of transaction characteristics (e.g. product type, wider range of collateral types) as well as borrower characteristics. This is required in order to ensure that should credit risk characteristics change there is appropriate re-segmentation of the assets. This may result in new portfolios being created or assets moving to an existing portfolio that better reflects the similar credit risk characteristics of that group of assets. Re-segmentation of portfolios and movement between portfolios is more common when there is a significant increase in credit risk (or when that significant increase reverses) and so assets move from 12-month to lifetime ECLs, or vice versa, but it can also occur within portfolios that continue to be measured on the same basis of 12-month or lifetime ECLs but the amount of ECL changes because the credit risk of the portfolios differ.

Classification and measurement, de-recognition, and impairment of financial instruments effective prior to 1 January 2018

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability of another entity. Financial instruments are classified as follows:

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

Classification and measurement, de-recognition, and impairment of financial instruments effective prior to 1 January 2018 (continued)

(i) 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, goods and services directly to a debtor, with no intention of trading the receivable. Loans and receivables comprise loans and advances, placements with other banks, other assets (items in transit) and cash and bank balances.

(ii) Held-to-maturity

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

(iii) Recognition and measurement

The Group initially recognises loans and advances, deposits and debt securities issues on the date at which they are originated. All other financial assets and liabilities (including assets designated at fair value through the income statement) are initially recognized on the trade date, which is the date the Group becomes party to the contractual provisions of the instrument.

A financial asset or financial liability is initially measured at fair value plus, for items not at fair value through profit or loss, translation costs are directly attributable to the acquisition or issue.

Subsequent to initial recognition, financial liabilities (deposits and debt securities) are measured at their amortised cost using the effective rate method except where the Group design liabilities at fair value through profit or loss.

(iv) De-recognition

A financial asset is derecognised when the Group loses control over the contractual rights that comprise that asset. This occurs when the rights are realised, expire or are surrendered. A financial liability is derecognised when its contractual obligations are discharged or cancelled or expire.

On de-recognition of a financial asset, the difference between the carrying amount of the asset and the consideration received is recognised in profit or loss.

Held-to-maturity instruments and originated loans and receivables are derecognised on the day they are repaid in full or when they are transferred by the Group to a third party.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

Classification and measurement, de-recognition, and impairment of financial instruments effective prior to 1 January 2018 (continued)

(v) Identification and measurement of impairment of financial assets

At each reporting 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 that 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 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.

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

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Financial assets and liabilities (continued)

Classification and measurement, de-recognition, and impairment of financial instruments effective prior to 1 January 2018 (continued)

(vi) Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

(vii) Other financial liabilities

The Group classifies financial liabilities as other financial liabilities at amortised cost. Other financial liabilities include customer deposits, borrowings and deposits from banking and non-banking financial institutions.

(j) Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets other than 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 asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in the profit or loss. Impairment losses recognised in respect of cash-generating units 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.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(k) Dividends

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

(l) Contingent liabilities

Significant litigations and claims against the Group, letters of credit, acceptances, guarantees and performance bonds are accounted for and disclosed as contingent liabilities. Estimates of the outcome and the financial effect of contingent liabilities is made by management based on the information available up to the date the financial statements are approved for issue by the Directors. Any expected loss is recognised in profit or loss.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

(m) Fiduciary activities

Assets held for clients in an agency or fiduciary capacity by the Group are not assets of the Group and have a nil effect in the statement of financial position.

(n) Earnings per share

Earnings per share is calculated based on the profit attributable to shareholders divided by the weighted 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 period. During the period there were no significant outstanding shares with dilutive potential.

(o) New standards, amendments and interpretations

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

The Group has adopted the following new standards and amendments during the year ended 31 December 2018, including consequential amendments to other standards with the date of initial application by the Group being 1 January 2018. The nature and effects of the changes are as explained herein.

New standard or amendments	Effective for annual periods beginning on or after
IFRS 15 Revenue from Contracts with Customers	1 January 2018
IFRS 9 Financial Instruments (2014)	1 January 2018
Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2)	1 January 2018
Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4)	1 January 2018
IFRIC 22 Foreign Currency Transactions and Advance Consideration	1 January 2018
IAS 40 Transfers of Investment Property	1 January 2018
Annual improvements cycle (2014-2016)	1 January 2018

– IFRS 15 Revenue from Contracts with Customers

I FRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations. Under IFRS 15, revenue is recognised when a customer obtains control of the goods or services. Determining the timing of the transfer of control – at a point in time or over time – requires judgment.

The Group has adopted IFRS 15 using the cumulative effect method (without practical expedients), with the effect of initially applying this standard recognised at the date of initial application (i.e. 1 January 2018). Accordingly, the information presented for 2017 has not been restated – i.e. it is presented, as previously reported, under IAS 18, IAS 11 and related interpretations. Additionally, the disclosure requirements in IFRS 15 have not generally been applied to comparative information.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

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

– *IFRS 15 Revenue from Contracts with Customers (Continued)*

The following table summarises the impact, net of tax, of transition to IFRS 15 on retained earnings and OCI at 1 January 2018.

	Impact of adopting IFRS 15 at 1 January 2018
Retained earnings	**Kshs '000'**
Trade Receivables	(600,147)
Housing Development Projects	841,174
House sale Deposits	(410,310)
	(169,283)
Adjustments on initial application of IFRS 15 on joint ventures (net of tax)	(31,508)
Total adjustments on initial application of IFRS 15	**(200,791)**
Related tax	50,785
Impact at 1 January 2018 net of tax	**(150,006)**

The following tables summarise the impacts of adopting IFRS 15 on the Group's statement of financial position as at 31 December 2017 and its statement of profit or loss and OCI for the year then ended for each of the line items affected. There was no material impact on the Group's statement of cash flows for the year ended 31 December 2017.

Impact on the consolidated statement of financial position

	As reported	Adjustments	Amounts on adoption of IFRS 15
Assets	**Kshs '000'**	**Kshs '000'**	**Kshs '000'**
Other assets	1,487,808	(600,147)	887,661
Housing Development Projects	2,414,469	841,174	3,255,643
Tax Recoverable	204,012	50,785	254,797
Investment in Joint ventures	1,713,985	(31,508)	1,682,477
Others	61,720,842	-	61,720,842
Total assets	**67,541,116**	**260,304**	**67,801,420**
Equity			
Retained Earnings	108,398	(150,006)	(41,608)
Others	11,341,137	-	11,341,137
Total equity	**11,449,535**	**(150,006)**	**11,299,529**
Liabilities			
House sale Deposits	124,118	410,310	534,428
Others	55,967,463	-	55,967,463
Total liabilities	**56,091,581**	**410,310**	**56,501,891**
Total equity and liabilities	**67,541,116**	**260,304**	**67,801,420**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

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

– *IFRS 15 Revenue from Contracts with Customers (Continued)*

Impact on the consolidated statement of profit or loss and OCI

For the year ended 31 December 2017	As reported	Adjustments	Amounts on adoption of IFRS 15
	Kshs '000	Kshs '000	Kshs '000
Non-interest income	1,346,426	(1,010,457)	335,969
Non interest expense	(3,412,196)	841,174	(2,571,022)
Income tax expense	(185,408)	50,785	(134,623)
Others	2,377,394	(118,498)	2,258,896
Profit for the period	**126,216**	**(236,996)**	**(110,780)**
Total comprehensive income for the period	**333,460**	**50,785**	**384,245**

IFRS 15 did not have a significant impact on the Group's accounting policies with respect to other revenue streams. For additional information about the Group's accounting policies relating to revenue recognition, see Note 8.

Transition

The Group and Company applied IFRS 15 on 1 January 2018 using the modified retrospective approach in which the cumulative effect of initially applying this Standard is recognised at the date of initial application as an adjustment to the opening balance of retained earnings as at 1 January 2018 without restating comparative periods.

– *IFRS 9: Financial Instruments (2014)*

On 24 July 2014 the IASB issued the final IFRS 9 Financial Instruments Standard. IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy and sell non-financial items. The Standard replaces earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement.

The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

As a result of the adoption of IFRS 9, the Group has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures about 2018, but have not been applied to the comparative information.

The key changes to the Group's accounting policies resulting from its adoption of IFRS 9 are summarised below. The full impact of adopting the standard is set out in Note 4.

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL).

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

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

– IFRS 9: Financial Instruments (2014) - continued

IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows.

The standard eliminates the previous IAS 39 categories of held-to-maturity, Loans and advances and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification. For an explanation of how the Group classifies financial assets under IFRS 9, see Note 4(a).

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

(a) the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in other comprehensive income ; and

(b) the remaining amount of change in the fair value is presented in profit or loss.

For an explanation of how the Group classifies financial liabilities under IFRS 9, see Note 3(i).

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

Comparative periods generally have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9. The Group used the exemption not to restate comparative periods.

The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

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

– IFRS 9: Financial Instruments (2014) - continued

(a) The determination of the business model within which a financial asset is held.

(b) Determination of factors to consider in determining whether there has been a significant increase in credit risk.

(c) If a debt security had low credit risk at the date of initial application of IFRS 9, then the Group has assumed that credit risk on the asset had not increased significantly since its initial recognition.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, refer to Note 4.

– Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2)

The following clarifications and amendments are contained in the pronouncement:

• Accounting for cash-settled share-based payment transactions that include a performance condition

Up until this point, IFRS 2 contained no guidance on how vesting conditions affect the fair value of liabilities for cash-settled share-based payments. IASB has now added guidance that introduces accounting requirements for cash-settled share-based payments that follows the same approach as used for equity-settled share-based payments.

• Classification of share-based payment transactions with net settlement features

IASB has introduced an exception into IFRS 2 so that a share-based payment where the entity settles the share-based payment arrangement net is classified as equity-settled in its entirety provided the share-based payment would have been classified as equity-settled had it not included the net settlement feature.

• Accounting for modifications of share-based payment transactions from cash-settled to equity-settled

Up until this point, IFRS 2 did not specifically address situations where a cash-settled share-based payment changes to an equity-settled share-based payment because of modifications of the terms and conditions. The IASB has introduced the following clarifications:

(i) On such modifications, the original liability recognised in respect of the cash-settled share-based payment is derecognised and the equity-settled share-based payment is recognised at the modification date fair value to the extent services have been rendered up to the modification date.

(ii) Any difference between the carrying amount of the liability as at the modification date and the amount recognised in equity at the same date would be recognised in profit and loss immediately.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

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

– Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2) - continued

The amendments were effective for annual periods beginning on or after 1 January 2018. Earlier application was permitted. The amendments were to be applied prospectively. However, retrospective application was allowed if possible without the use of hindsight. If an entity applies the amendments retrospectively, it must do so for all of the amendments described above.

The adoption of this standard did not have a material impact on the Group's financial statements.

– Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4)

The amendments in Applying IFRS 9 'Financial Instruments' with IFRS 4 'Insurance Contracts' (Amendments to IFRS 4) provide two options for entities that issue insurance contracts within the scope of IFRS 4:

(a) an option that permits entities to reclassify, from profit or loss to other comprehensive income, some of the income or expenses arising from designated financial assets; this is the so-called overlay approach;
(b) an optional temporary exemption from applying IFRS 9 for entities whose predominant activity is issuing contracts within the scope of IFRS 4; this is the so-called deferral approach.

The application of both approaches is optional and an entity is permitted to stop applying them before the new insurance contracts standard is applied.

An entity applies the overlay approach retrospectively to qualifying financial assets when it first applies IFRS 9. Application of the overlay approach requires disclosure of sufficient information to enable users of financial statements to understand how the amount reclassified in the reporting period is calculated and the effect of that reclassification on the financial statements.

An entity applies the deferral approach for annual periods beginning on or after 1 January 2018. Predominance is assessed at the reporting entity level at the annual reporting date that immediately precedes 1 April 2016. Application of the deferral approach needs to be disclosed together with information that enables users of financial statements to understand how the insurer qualified for the temporary exemption and to compare insurers applying the temporary exemption with entities applying IFRS 9. The deferral can only be made use of for the three years following 1 January 2018. Predominance is only reassessed if there is a change in the entity's activities.

The adoption of this standard did not have a material impact on the Group's financial statements.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

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

– IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration

This Interpretation applies to a foreign currency transaction (or part of it) when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognises the related asset, expense or income (or part of it).

This Interpretation stipulates that the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.

This Interpretation does not apply to income taxes, insurance contracts and circumstances when an entity measures the related asset, expense or income on initial recognition:

(i) at fair value; or

(ii) at the fair value of the consideration paid or received at a date other than the date of initial recognition of the non-monetary asset or non-monetary liability arising from advance consideration (for example, the measurement of goodwill applying IFRS 3 Business Combinations).

The amendments apply retrospectively for annual periods beginning on or after 1 January 2018, with early application permitted.

The adoption of this interpretation did not have a material impact on the Group's financial statements.

– Transfers of Investment property (Amendments to IAS 40)

The IASB has amended the requirements in IAS 40 Investment property on when a company should transfer a property asset to, or from, investment property.

During the year, the Group transferred HF Development and Investment Limited building (Kshs. 748,549,115), previously classified under investment property, to property and equipment.

– Annual improvement cycle (2014 – 2016) – various standards

Standards	**Amendments**
IFRS 1 First-time time Adoption of IFRS	Outdated exemptions for first-time adopters of IFRS are removed. The amendments apply prospectively for annual periods beginning on or after 1 January 2018.
IAS 28 Investments in Associates and Joint Ventures	A venture capital organisation, or other qualifying entity, may elect to measure its investments in an associate or joint venture at fair value through profit or loss. This election can be made on an investment-by-investment basis. A non-investment entity investor may elect to retain the fair value accounting applied by an investment entity associate or investment entity joint venture to its subsidiaries. This election can be made separately for each investment entity associate or joint venture. The amendments apply retrospectively for annual periods beginning on or after 1 January 2018; early application is permitted.

The adoption of these standards did not have a material impact on the amounts and disclosures of the Group's financial statements.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2018, and have not been applied in preparing these financial statements.

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

• IFRS 16 Leases	1 January 2019
• IFRIC 23 Uncertainty over income tax treatments	1 January 2019
• IFRS 9 Prepayment Features with Negative Compensation	1 January 2019
• IAS 28 Long-term Interests in Associates and Joint Ventures	1 January 2019
• Annual improvements cycle (2015-2017)	1 January 2019
• IAS 19 Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)	1 January 2019
• IFRS 3 Definition of a Business	1 January 2020
• Amendments to references to the Conceptual Framework in IFRS Standards	1 January 2020
• Amendments to IAS 1 and IAS 8 Definition of Material	1 January 2020
• IFRS 17 Insurance contracts	1 January 2022
• Sale or Contribution of Assets between an Investor and its Associate or Group (Amendments to IFRS 10 and IAS 28).	To be determined

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

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 (Continued)

– IFRS 16: Leases

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

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

A company assesses whether a contract contains a lease on the basis of whether the customer has the right to control the use of an identified asset for a period of time.

The standard eliminates the classification of leases as either operating leases or finance leases for a lessee and introduces a single lessee accounting model. All leases are treated in a similar way to finance leases.

Applying that model significantly affects the accounting and presentation of leases and consequently, the lessee is required to recognise:

assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A company recognises the present value of the unavoidable lease payments and shows them either as lease assets (right-of-use assets) or together with property, plant and equipment. If lease payments are made over time, a company also recognises a financial liability representing its obligation to make future lease payments.

- depreciation of lease assets and interest on lease liabilities in profit or loss over the lease term; and
- separate the total amount of cash paid into a principal portion (presented within financing activities) and interest (typically presented within either operating or financing activities) in the statement of cash flows

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

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

— short-term leases (i.e. leases of 12 months or less) and;
— leases of low-value assets

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

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 - continued

–IFRS 16: Leases - continued

As at 31 December 2018 the Group future operating lease payments amounted to Kshs 238m on a discounted basis which the Group estimates it will recognize as additional lease liability and right-of-use asset on its financial statements at 1 January 2019.

– IFRIC 23 Clarification on accounting for Income tax exposures

IFRIC 23 clarifies the accounting for income tax treatments that have yet to be accepted by tax authorities, whilst also aiming to enhance transparency.

IFRIC 23 explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.

An uncertain tax treatment is any tax treatment applied by an entity where there is uncertainty over whether that treatment will be accepted by the tax authority.

If an entity concludes that it is probable that the tax authority will accept an uncertain tax treatment that has been taken or is expected to be taken on a tax return, it should determine its accounting for income taxes consistently with that tax treatment. If an entity concludes that it is not probable that the treatment will be accepted, it should reflect the effect of the uncertainty in its income tax accounting in the period in which that determination is made. Uncertainty is reflected in the overall measurement of tax and separate provision is not allowed.

The entity is required to measure the impact of the uncertainty using the method that best predicts the resolution of the uncertainty (that is, the entity should use either the most likely amount method or the expected value method when measuring an uncertainty).

The entity will also need to provide disclosures, under existing disclosure requirements, about

(a) judgments made;
(b) assumptions and other estimates used; and
(c) potential impact of uncertainties not reflected.

The new Standard is effective for annual periods beginning on or after 1 January 2019.

The Group is assessing the potential impact on its financial statements resulting from the application of IFRIC 23.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 - continued

– Prepayment Features with Negative Compensation (Amendments to IFRS 9)

The amendments clarify that financial assets containing prepayment features with negative compensation can now be measured at amortised cost or at fair value through other comprehensive income (FVOCI) if they meet the other relevant requirements of IFRS 9.

The amendments apply for annual periods beginning on or after 1 January 2019 with retrospective application, early adoption is permitted.

The adoption of these amendments will not have an impact on the financial statements of the Group.

– Long-term Interests in Associates and Joint Ventures (Amendment to IAS 28)

The amendments clarify that an entity applies IFRS 9 to long-term interests in an associate and joint venture that form part of the net investment in the associate or joint venture but to which the equity method is not applied.

The amendments apply for annual periods beginning on or after 1 January 2019. Early adoption is permitted.

The adoption of these standards will not have an impact on the financial statements of the Group.

– Annual improvement cycle (2015 – 2017) – various standards

Standards	Amendments
IFRS 3 Business Combinations and IFRS 11 Joint Arrangements	Clarifies how a company accounts for increasing its interest in a joint operation that meets the definition of a business: – If a party maintains (or obtains) joint control, then the previously held interest is not remeasured. – If a party obtains control, then the transaction is a business combination achieved in stages and the acquiring party remeasures the previously held interest at fair value
IAS 12 Income taxes	Clarifies that all income tax consequences of dividends (including payments on financial instruments classified as equity) are recognised consistently with the transactions that generated the distributable profits – i.e. in profit or loss, OCI or equity.
IAS 23 Borrowing costs	Clarifies that the general borrowings pool used to calculate eligible borrowing costs excludes only borrowings that specifically finance qualifying assets that are still under development or construction. Borrowings that were intended to specifically finance qualifying assets that are now ready for their intended use or sale – or any non-qualifying assets – are included in that general pool. As the costs of retrospective application might outweigh the benefits, the changes are applied prospectively to borrowing costs incurred on or after the date an entity adopts the amendments.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 - continued

– Annual improvement cycle (2015 – 2017) – various standards - continued

The amendments are effective for annual reporting periods beginning on or after 1 January 2019 with earlier application permitted. The adoption of these amendments is not expected to affect the amounts and disclosures of the Group's financial statements.

– IAS 19 Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)

The amendments clarify that:

- on amendment, curtailment or settlement of a defined benefit plan, a Group now uses updated actuarial assumptions to determine its current service cost and net interest for the period; and
- the effect of the asset ceiling is disregarded when calculating the gain or loss on any settlement of the plan and is dealt with separately in other comprehensive income (OCI).

Consistent with the calculation of a gain or loss on a plan amendment, entities will now use updated actuarial assumptions to determine the current service cost and net interest for the period. Previously, entities would not have updated the calculation of these costs until the year-end.

Further, if a defined benefit plan is settled, any asset ceiling would be disregarded when determining the plan assets as part of the calculation of gain or loss on settlement.

The amendments apply for plan amendments, curtailments or settlements that occur on or after 1 January 2019, or the date on which the amendments are first applied. Earlier application is permitted.

The adoption of this standard will not have an impact on the financial statements of the Group.

– IFRS 3 Definition of a Business

With a broad business definition, determining whether a transaction results in an asset or a business acquisition has long been a challenging but important area of judgement. These amendments to IFRS 3 Business Combinations seek to clarify this matter as below however complexities still remain.

- Optional concentration test

  The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets.

- Substantive process

  If an entity chooses not to apply the concentration test, or the test is failed, then the assessment focuses on the existence of a substantive process.

The definition of a business is now narrower and could result in fewer business combinations being recognised.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 - continued

– IFRS 3 Definition of a Business - continued

The amendment applies to businesses acquired in annual reporting periods beginning on or after 1 January 2020. Earlier application is permitted.

– Amendments to References to the Conceptual Framework in IFRS Standards

This amendment sets out amendments to IFRS Standards (Standards), their acGrouping documents and IFRS practice statements to reflect the issue of the International Accounting Standards Board (IASB) revised Conceptual Framework for Financial Reporting in 2018 (2018 Conceptual Framework).

Some Standards, their accompanying documents and IFRS practice statements contain references to, or quotations from, the IASC's Framework for the Preparation and Presentation of Financial Statements adopted by the IASB in 2001 (Framework) or the Conceptual Framework for Financial Reporting issued in 2010. Amendments to References to the Conceptual Framework in IFRS Standards updates some of those references and quotations so that they refer to the 2018 Conceptual Framework, and makes other amendments to clarify which version of the Conceptual Framework is referred to in particular documents.

These amendments are based on proposals in the Exposure Draft Updating References to the Conceptual Framework, published in 2015, and amend

Standards, their accompanying documents and IFRS practice statements that will be effective for annual reporting periods beginning on or after 1 January 2020.

The adoption of these changes will not affect the amounts and disclosures of the Group's financial statements.

– IAS 1 and IAS 8 Definition of Material

The amendment refines the definition of Material to make it easier to understand and aligning the definition across IFRS Standards and the Conceptual Framework.

The amendment includes the concept of 'obscuring' to the definition, alongside the existing references to 'omitting' and 'misstating'. Additionally, the amendment also adds the increased threshold of 'could influence' to 'could reasonably be expected to influence' as below.

"Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity."

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 - continued

– IAS 1 and IAS 8 Definition of Material - continued

However, the amendment has also removed the definition of material omissions or misstatements from IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

The amendments are effective from 1 January 2020 but may be applied earlier.

The Group is assessing the potential impact on its financial statements resulting from the application of the refined definition of materiality.

– IFRS 17 Insurance Contracts

IFRS 17 Insurance Contracts sets out the requirements that an entity should apply in reporting information about insurance contracts it issues and reinsurance contracts it holds. An entity shall apply IFRS 17 Insurance Contracts to:

- insurance contracts, including reinsurance contracts, it issues;
- reinsurance contracts it holds; and
- investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts.

IFRS 17 requires an entity that issues insurance contracts to report them on the statement of financial position as the total of:

- the fulfilment cash flows—the current estimates of amounts that the entity expects to collect from premiums and pay out for claims, benefits and expenses, including an adjustment for the timing and risk of those amounts; and
- the contractual service margin—the expected profit for providing insurance coverage. The expected profit for providing insurance coverage is recognised in profit or loss over time as the insurance coverage is provided.

IFRS 17 requires an entity to recognise profits as it delivers insurance services, rather than when it receives premiums, as well as to provide information about insurance contract profits that the Group expects to recognise in the future. IFRS 17 requires an entity to distinguish between groups of contracts expected to be profit making and groups of contracts expected to be loss making. Any expected losses arising from loss-making, or onerous contracts are accounted for in profit or loss as soon as the Group determines that losses are expected. IFRS 17 requires the entity to update the fulfilment cash flows at each reporting date, using current estimates of the amount, timing and uncertainty of cash flows and of discount rates. The entity:

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(o) New standards, amendments and interpretations (continued)

(ii) New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2018 - continued

– IFRS 17 Insurance Contracts - continued

- accounts for changes to estimates of future cash flows from one reporting date to another either as an amount in profit or loss or as an adjustment to the expected profit for providing insurance coverage, depending on the type of change and the reason for it; and
- chooses where to present the effects of some changes in discount rates—either in profit or loss or in other comprehensive income.

IFRS 17 also requires disclosures to enable users of financial statements to understand the amounts recognised in the entity's statement of financial position and statement of profit or loss and other comprehensive income, and to assess the risks the Group faces from issuing insurance contracts.

IFRS 17 replaces IFRS 4 Insurance Contracts. IFRS 17 is effective for financial periods commencing on or after 1 January 2022. An entity shall apply the standard retrospectively unless impracticable. A Company can choose to apply IFRS 17 before that date, but only if it also applies IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers.

The adoption of these changes will not affect the amounts and disclosures of the Group's financial statements.

– Sale or Contribution of Assets between an Investor and its Associate or Company (Amendments to IFRS 10 and IAS 28)

The amendments require the full gain to be recognised when assets transferred between an investor and its associate or Company meet the definition of a 'business' under IFRS 3 Business Combinations. Where the assets transferred do not meet the definition of a business, a partial gain to the extent of unrelated investors' interests in the associate or Company is recognised. The definition of a business is key to determining the extent of the gain to be recognised.

The effective date for these changes has now been postponed until the completion of a broader review.

The adoption of these changes will not affect the amounts and disclosures of the Group's financial statements.

The Group did not early adopt new or amended standards in the year ended 31 December 2018.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT

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

(i) credit risk

(ii) liquidity risk

(iii) market risk

(iv) capital management

The Directors have overall responsibility for the establishment and oversight of the Group's risk management framework. The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

(a) Credit risk

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

Management of credit risk

Assessment (policy applicable before 1 January 2018)

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

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's loans and advances to customers and other banks, and investment debt securities. For risk management reporting purposes, the Group considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Credit risk is the Group's largest risk and considerable resources, expertise and controls are devoted to managing it and comprehensive strategies, policies and procedures have been developed to effectively manage this risk.

The Board provides effective oversight of the overall credit portfolio through the Board Credit Committee (BCC). This committee is the decision making body with responsibility for loans that exceed the scope of authority of the management lending committee. Acting on the basis of the powers granted to it by the Board, the BCC decides on the overall lending limits for the Group and approves the credit risk strategies to be adopted.

The Group has adequate Board approved Credit Policies which are reviewed annually and which cover all aspects of credit risk management (loan origination, analysis and appraisal, acceptable collateral, approval authorities and non-performing loan management).

At the management level, there is a Credit Risk Department staffed with highly skilled personnel who ensure credit risks are identified and mitigated. Within this department there is a fully fledged loan recoveries and rehabilitation unit with the responsibility of formulating workout solutions and restructuring loans in distress.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Management of credit risk (Continued)

The Group's primary exposure to credit risk arises through its loan advances to customers. The amount of credit exposure in this regard is represented by the carrying amounts of the assets on the statement of financial position. 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 statement of financial position.

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 obtains collateral.

The Group also monitors concentration of credit risk that arises by customer in relation to loan advances to customers. The Group largest exposure to customers are within the statutory limit.

Impaired loan advances

Impaired loans and securities are loans and advances for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan. These loans are graded as substandard to loss categories in the Group's internal credit risk grading system.

Past due but not impaired loans

Past due but not impaired loans are those for which contractual interest or principal payments are past due but not for more than three months and the Group believes that impairment is not appropriate on the basis that in the Group's assessment the total outstanding balances are recoverable and the level of security / collateral available and / or the stage of collection of amounts owed to the Group is adequate. Any amounts past due for more than three months are considered impaired.

Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Group has made concessions that it would not otherwise consider. Once the loan is restructured it remains in this category until satisfactory performance after restructuring.

Allowances for impairment

The Group establishes an allowance for impairment losses on assets carried at amortised cost or classified as available for sale that represents its estimate of incurred losses in its loan and investment debt security portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loan loss allowance established for a group of homogeneous assets in respect of losses that have been incurred but have not been identified on loans that are considered individually insignificant as well as individually significant exposures that were subject to individual assessment for impairment but not found to be individually impaired.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Write-off policy

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

An estimate of the fair values of collateral against loans and advances to customers is shown below:

	2018	2017
	KShs'000	KShs'000
Against impaired accounts	23,647,226	13,189,667
Against accounts not impaired	114,899,354	152,152,075
	138,546,580	**165,341,742**

Details of financial and non-financial assets obtained by the Group during the period by taking possession of collateral held against loans and advances held at the period-end are shown below:

	2018	2017
	KShs'000	KShs'000
Properties	138,217,734	165,165,066
Secured by cash	328,846	176,676
	138,546,580	**165,341,742**

The Group's policy is to pursue timely realisation of the collateral in an orderly manner.

The Group holds collateral against loans and advances to customers in the form of mortgage interests over property. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral is not held over placements with banks and investment in government securities as these are considered to be risk free.

Credit related commitments risk

The Group makes available to its customers guarantees that may require that the Group makes payments on their behalf and enters into commitments to extend credit lines to secure their liquidity needs. Letters of credit and guarantees (including standby letters of credit) commit the Group to make payments on behalf of customers in the event of a specific act, generally related to the import or export of goods. Such commitments expose the Group to similar risks to loans and are mitigated by the same control processes and policies.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Assessment (Policy applicable from 1 January 2018)

The references below show where the Group's impairment assessment and measurement approach is set out in this report. It should be read in conjunction with the Summary of significant accounting policies.

Definition of default

The Group considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments. The Group considers treasury and intercompany balances defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

As a part of a qualitative assessment of whether a customer is in default, the Group also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Group carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate. Such events include:

- Internal rating of the borrower indicating default or near-default
- The borrower requesting emergency funding from the Group
- The borrower having past due liabilities to public creditors or employees
- The borrower is deceased
- A material decrease in the underlying collateral value where the recovery of the loan is expected from the sale of the collateral
- A material decrease in the borrower's turnover or the loss of a major customer
- A covenant breach not waived by the Group

The debtor (or any legal entity within the debtor's group) filing for bankrruptcy application/protection Debtor's listed debt or equity suspended at the primary exchange because of rumours or facts about financial difficulties

It is the Group's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least six consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

The Group's rating and PD estimation process

The Group rates its key portfolios from 1 to 3 using the Group's model rating. The models incorporate both qualitative and quantitative information and, in addition to information specific to the borrower, utilise supplemental external information that could affect the borrower's behaviour. Where practical, they also build on information from S&P Agency.

PDs are then adjusted for IFRS 9 ECL calculations to incorporate forward looking information and the IFRS 9 Stage classification of the exposure. This is repeated for each economic scenario as appropriate.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Exposure at default

The exposure at default (EAD) represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the obligor's ability to increase its exposure while approaching default and potential early repayments too.

To calculate the EAD for a Stage 1 loan, the Group assesses the possible default events within 12 months for the calculation of the 12months ECL. However, if a Stage 1 loan that is expected to default in the 12 months from the balance sheet date and is also expected to cure and subsequently default again, then all linked default events are taken into account. For Stage 2, Stage 3 and purchased or originated credit impaired (POCI) financial assets, the exposure at default is considered for events over the lifetime of the instruments.

The Group determines EADs by modelling the range of possible exposure outcomes at various points in time, corresponding the multiple scenarios. The IFRS 9 PDs are then assigned to each economic scenario based on the outcome of Group's models.

Loss given default

For loans portfolios, LGD values are assessed at least every three months by account managers and reviewed and approved by the Group's credit risk department. The credit risk assessment is based on a standardised LGD assessment framework that results in a certain LGD rate. These LGD rates take into account the expected EAD in comparison to the amount expected to be recovered or realised from any collateral held.

The Group segments its retail lending products into portfolios, based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and involves a wider set of transaction characteristics (e.g., product type, wider range of collateral types) as well as borrower characteristics.

Further recent data and forward-looking economic scenarios are used in order to determine the IFRS 9 LGD rate for each group of financial instruments. When assessing forward-looking information, the expectation is based on multiple scenarios. Examples of key inputs involve changes in, collateral values including property prices for mortgages, commodity prices, payment status or other factors that are indicative of losses in the group. The Group estimates regulatory and IFRS 9 LGDs on a different basis. Under IFRS 9, LGD rates are estimated for the Stage 1, Stage 2, Stage 3 and purchased or originated credit impaired (POCI) IFRS 9 segment of each asset class. The inputs for these LGD rates are estimated and, where possible, calibrated through back testing against recent recoveries. These are repeated for each economic scenario as appropriate.

Significant increase in credit risk

The Group continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12 months ECL or LTECL, the Group assesses whether there has been a significant increase in credit risk since initial recognition. The Group considers an exposure to have significantly increased in credit risk when the IFRS 9 lifetime PD has doubled since initial recognition and has increased by more than 20 bps a year.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Significant increase in credit risk (continued)

The Group also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming forborne. In certain cases, the Group may also consider that some events are a significant increase in credit risk as opposed to a default. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

When estimating ECLs on a collective basis for a group of similar assets the Group applies the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

Grouping financial assets measured on a collective basis

The Group calculates ECLs either on a collective or an individual basis.

Asset classes where the Group calculates ECL on an individual basis include:

- All Stage 3 assets, regardless of the class of financial assets
- The Corporate lending portfolio
- The large and unique exposures of the Small business lending portfolio
- The treasury, trading and interbank relationships (such as due from Banks, Cash collateral on securities borrowed and reverse repurchase agreements and debt instruments at amortised cost/FVOCI
- Exposures that have been classified as POCI when the original loan was derecognised and a new loan was recognised as a result of a credit driven debt restructuring

Asset classes where the Group calculates ECL on a collective basis include:

- The smaller and more generic balances of the Group's Small business lending
- Stage 1 and 2 Retail mortgages and Consumer lending
- Purchased POCI exposures managed on a collective basis

The Group groups these exposure into smaller homogeneous portfolios, based on a combination of internal and external characteristics of the loans.

Analysis of inputs to the ECL model under multiple economic scenarios

The Group incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. On the basis of a variety of external actual and forecast information, the Group formulates a 'base case' view of the future direction of relevant economic variables as well as a representative range of other possible forecast scenarios. This process involves developing two additional economic scenarios and considering the relative probabilities of each outcome. External information includes economic data and forecasts published by governmental bodies and monetary authorities, other organisations such as the International Monetary Fund (IMF), World Bank and selected private-sector and academic forecasters.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Analysis of inputs to the ECL model under multiple economic scenarios (continued)

The base case represents a most-likely outcome and is aligned with information used by the Group for other purposes such as strategic planning and budgeting. The other scenarios represent more optimistic and more pessimistic outcomes. Periodically, the Group carries out stress testing of more extreme shocks to calibrate its determination of these other representative scenarios.

The Group has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables, credit risk and credit losses. The economic scenarios used as at 31 December 2018 included the following ranges of key indicators;

	Base Weighting	**Upside**	**Downside**
Macro-Economic Variable	75%	15%	10%
Central Bank rate	9.000%	11.580%	6.400%
Savings	4.670%	6.920%	2.410%
GDP	5.700%	6.350%	5.050%
Housing price index	0.390%	1.240%	(0.460%)
Public Debt to GDP	57.580%	64.83%	50.160%

The correlation of the above factors with the Group's non-performing loans (NPL %) were also used to determine whether these factors should be lagged.

Based on this analysis, Savings Rate was lagged by 3 months and Public debt to GDP ratio was lagged by 6 months.

The Group's non-performing loans (NPL%) was a reasonable approximation to the Group's default risk. The correlation between the Group's non-performing loans (NPL%) with the above macroeconomic factors was then inferred to the Group's predicated Probabilities of Default.

Further, in determining the economic scenarios to be applied, each of the economic variable was adjusted either upside or downside using the historical standard deviation.

In determining the likelihood of each of the three macroeconomic scenarios, a weighting of 90% (base case), 5% (upside case) and 5% (downside case) was applied.

Predicted relationships between the key indicators and default and loss rates on various portfolios of financial assets were developed based on analysing historical data over the past 3 to 5 years.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Measurement of ECL

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

— Probability of default (PD);
— Loss given default (LGD);
— Exposure at default (EAD).

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

PDs are estimates at a certain date, which are calculated based on statistical models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally compiled data comprising both quantitative and qualitative factors. Where it is available, market data may also be used to derive the PD for loans and advances to banks and investment securities.

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based mainly on the counterparties' collateral and also on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Group derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortisation. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount drawn, as well as potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts.

Contingent liabilities and commitments

To meet the financial needs of customers, the Group enters into various irrevocable commitments and contingent liabilities. These consist of financial guarantees, letters of credit and other commitments to lend. Even though these obligations may not be recognised on the statement of financial position, they contain credit risk and, therefore, form part of the overall risk of the Group.

Letters of credit and guarantees (including standby letters of credit) commit the Group to make payments on behalf of customers in the event of a specific act, generally related to the import or export of goods. Guarantees and standby letters of credit carry a similar credit risk to loans. The nominal values of such commitments are listed below:-

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Contingent liabilities and commitments - continued

	2018 KShs'000	2017 KShs'000
Undrawn overdrafts	485,125	308,190
Letters of credit	6,603	142,127
Guarantee	178,157	138,125
	669,885	**588,442**
Allowance for impairment losses	10,462	-

Impairment losses on guarantees and other commitments

The loss allowance on outstanding commitments and financial guaantees is carried in other liabilities and therefore no impact on the carrying amounts.

The tables below shows the credit quality and the maximum exposure to credit risk based on the Group's internal credit rating system and year-end stage classification. The amounts presented are gross of impairment allowances. An analysis of changes in the gross carrying amount and the corresponding allowance for impairment losses in relation to guarantees and other commitments is as follows:

Gross carrying amount

	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
Credit quality analysis on guarantees and other commitments					
Low risk	168,057	-	-	168,057	280,252
Higher risk	-	501,828	-	501,828	308,190
Net carrying amount at 31 December 2018	**168,057**	**501,828**	**-**	**669,885**	**588,442**
Loss allowance	981	9,481	-	10,462	-

Impairment losses	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
Impairment losses on guarantees and other commitments					
Adjusted balance at 1 January 2018	1,880	8,048	-	9,928	-
Transfer to 12 months ECL (Stage 1)	-	-	-	-	-
Transfer to Lifetime ECL not credit impaired (Stage 2)	(71)	71	-	-	-
Net re-measurement of loss allowance	(285)	(71)	-	(356)	-
New financial assets originated or purchased	33	1,499	-	1,532	-
Financial assets derecognised	(576)	(66)	-	(642)	-
Balance at 31 December 2018	**981**	**9,481**	**-**	**10,462**	-

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Gross carrying amount

	Stage 1	Stage 2	Stage 3	2018 Total	2017 Total
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Credit quality analysis on Loans and advances					
Normal	28,026,927	-	-	28,026,927	35,736,331
Watch	-	5,244,224	-	5,244,224	8,659,687
Substandard	-	-	2,712,455	2,712,455	915,317
Doubtful	-	-	10,621,901	10,621,901	7,296,850
Balance at 31 December 2018	**28,026,927**	**5,244,224**	**13,334,356**	**46,605,507**	**52,608,185**
Less loss allowance	(67,601)	(110,058)	(2,987,712)	(3,165,371)	(2,968,546)
Net carrying amount	**27,959,326**	**5,134,166**	**10,346,644**	**43,440,136**	**49,639,639**

The following tables show reconciliations from the opening to the closing balance of the loss allowance for loans and advances.

Impairment allowance for loans and advances

Loans and advances to customers at amortised cost	12 month ECL (Stage 1)	Lifetime ECL not credit impaired (Stage 2)	Lifetime ECL credit impaired (Stage 3)	Total
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**
Adjusted balance at 1 January	301,604	105,998	2,844,920	3,252,522
Transfer to 12 months ECL (Stage 1)	107,505	(22,031)	(85,474)	-
Transfer to Lifetime ECL not credit impaired (Stage 2)	(48,925)	159,088	(110,163)	-
Transfer to Lifetime ECL credit impaired (Stage 3)	(112,755)	(368,782)	481,537	-
Net re-measurement of loss allowance	15,112	224,234	32,408	271,754
New financial assets originated or purchased	9,197	12,321	96,486	118,004
Financial assets derecognised	(204,137)	(770)	(272,002)	(476,909)
Balance at 31 December 2018	**67,601**	**110,058**	**2,987,712**	**3,165,371**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Impairment allowance for loans and advances - continued

2017:	Impairment Losses KShs'000	Portfolio Impairment KShs'000	Total KShs'000
At 1 January 2017	2,421,649	123,492	2,545,141
Impairment made in the year	1,098,622	-	1,098,622
Provisions no longer required	(521,067)	(1,352)	(522,419)
Written off against balance	(152,798)	-	(152,798)
At 31 December 2017	**2,846,406**	**122,140**	**2,968,546**

Balances with commercial banks

The following table sets out credit quality analysis for balances with commercial banks.

Balances with commercial banks at amortised cost	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
Low risk	137,373	-	-	137,373	808,625
Loss allowance	(642)	-	-	(642)	-
Net carrying amount	**136,731**	**-**	**-**	**136,731**	**808,625**

The following tables show reconciliations from the opening to the closing balance of the loss allowance for balances with commercial banks.

	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
ECL allowance as at 1 January 2018	508	-	-	508	508
Net remeasurement	134	-	-	134	-
Balance as at 31 December	**642**	**-**	**-**	**642**	**-**

Balances with Central Bank of Kenya

An analysis of credit quality analysis in the gross carrying amount and the corresponding ECL allowances is, as follows:

Balances with Central bank of Kenya at amortised cost	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
Low risk	2,423,468	-	-	2,423,468	2,823,459
Balance as at 31 December	**2,423,468**	**-**	**-**	**2,423,468**	**2,823,459**
Less loss allowance	-	-	-	-	-
Net carrying amount	**2,423,468**	**-**	**-**	**2,423,468**	**2,823,459**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Placements with other banks

An analysis of credit quality analysis in the gross carrying amount and the corresponding ECL allowances is as follows:

Placements with other banks

	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
Low risk	1,904,995	-	-	1,904,995	1,492,637
Balance as at 31 December 2018	**1,904,995**	-	-	**1,904,995**	**1,492,637**
Loss allowance	(300)	-	-	(300)	-
Net carrying amount	**1,904,695**	-	-	**1,904,695**	**1,492,637**

The following tables show reconciliations from the opening to the closing balance of the loss allowance for balances with placement with other banks.

Loss allowance	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
ECL allowance as at 1 January 2018	601	-	-	601	-
Net remeasurement	(301)	-	-	(301)	-
Balance as at 31 December 2018	**300**	-	-	**300**	-

Government Securities

An analysis of credit quality analysis in the gross carrying amount and the corresponding ECL allowances is as follows:

Gorverment securities	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	2018 Total KShs'000	2017 Total KShs'000
Held at amortised cost: Low risk	515,801	-	-	515,801	-
Held at FVOCI: Low risk	2,696,339	-	-	2,696,339	-
Held to maturity	-	-	-	-	746,179
Held as available for sale	-	-	-	-	1,541,117
Balance as at 31 December	3,212,140	-	-		2,287,296
Loss allowance	-	-	-	-	-
Net carrying amount	**3,212,140**	-	-		**2,287,296**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (continued)

Other receivables

An analysis of changes in the gross carrying amount and the corresponding ECL allowances is as follows:

	Stage 1	Stage 2	Stage 3	2018 Total	2017 Total
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Low risk	419,451	38,364	90,174	547,989	837,244
Balance at 31 Dcember 2018	**419,451**	**38,364**	**90,174**	**547,989**	**837,244**
Loss allowance	(26,698)	(27,292)	(82,588)	(136,578)	-
Net carrying amount	**392,753**	**11,072**	**7,586**	**411,411**	**837,244**

The following tables show reconciliations from the opening to the closing balance of the loss allowance for other assets.

	Stage 1	Stage 2	Stage 3	2018 Total	2017 Total
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
ECL allowance as at 1 January 2018	20,763	18,221	26,064	65,048	-
Net remeasurement	5,935	9,071	56,524	71,530	-
	26,698	**27,292**	**82,588**	**136,578**	**-**

(b) Classification of financial assets and financial liabilities on the date of initial application of IFRS 9

The application of the Group's policies in line with IFRS 9 did not result in any reclassification.

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Group's financial assets and financial liabilities as at 1 January 2018

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(b) Classification of financial assets and financial liabilities on the date of initial application of IFRS 9 (Continued)

	Original classfication under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	Original carrying amount under IFRS 9	Difference
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Financial assets					
Cash and balances with Banks	Amortised cost	Amortised cost	4,079,347	4,078,840	**508**
Placements with other banks	Amortised cost	Amortised cost	1,492,637	1,492,036	**601**
Gorverment securities:					
From held to maturity	Held to maturity	Amortised cost	746,179	746,179	**-**
From available for sale	available for sale	FVOCI	1,541,117	1,541,117	**-**
Loans and advances to customers	Loans and advances	Amortised cost	49,368,686	49,084,907	**283,779**
Loans and advances to banks	Loans and advances	Amortised cost	270,953	270,756	**197**
Other assets	Amortised cost	Amortised cost	837,244	772,196	**65,048**
Guarantees and letters of credit			588,442	578,514	**9,928**
Total			**58,924,605**	**58,564,544**	**360,061**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(b) Classification of financial assets and financial liabilities on the date of initial application of IFRS 9 (Continued)

	IAS 39 carrying amount 31 December 2017	Reclassfication	Re-measurement	IFRS 9 carrying amount 1 January 2018
	KShs'000	KShs'000	KShs'000	KShs'000
Financial assets				
Cash and balances with Banks				
Opening balance	4,079,347			
Re-measurement			(508)	
Closing balance				**4,078,839**
Placements with other banks				
Opening balance	1,492,637			
Re-measurement			(601)	
Closing balance				**1,492,036**
Gorverment securities:				
Opening balance	2,287,296			
To amortised cost		(746,179)		
To FVOCI		(1,541,117)		
Closing balance				
Amortised cost				
Gorverment securities:				
Opening balance				
To amortised cost		746,179		
Closing balance				**746,179**
FVOCI				
Gorverment securities:				
Opening balance				
To FVOCI		1,541,117		
Closing balance				**1,541,117**
Loans and advances to customers	49,368,686			
Loans and advances to banks	270,953			
Re-measurement			(283,976)	
Closing balance				**49,355,663**
Other assets	837,244		(65,048)	772,196
Off balance sheet	588,442		(9,928)	578,514
Total	**58,924,605**		**(360,061)**	**58,263,467**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(b) Classification of financial assets and financial liabilities on the date of initial application of IFRS 9 (Continued)

The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018.

	IAS 39 carrying amount 31 December 2017	Re-measurement	IFRS 9 carrying amount 1 January 2018
Financial liabilities	**KShs'000**	**KShs'000**	**KShs'000**
Amortised cost			
Deposits from customer	36,660,581	-	36,660,581
Deposits from banks	83,692	-	83,692
Borrowings	12,991,306	-	12,991,306
Corporate bond	3,047,369		3,047,369
Other liabilities	3,308,630	-	3,308,630
Total amortised cost	**56,091,578**	-	**56,091,578**

Impact of transition of IFRS 9 on opening equity reserves

The following table summarises the impact of transition to IFRS 9 on the opening balance of the retained earnings and the statutory credit risk reserve. There is no impact on other components of equity.

	Impact on initial application of IFRS 9 and IFRS 15
	KShs'000
Statutory credit risk reserve	
Closing balance under IAS 39 (31 December 2017)	640,800
IFRS 9 transition adjustment for CBK additional provisions no longer required	(283,976)
Related tax	-
Opening balance under IFRS 9 (1 January 2018)	
Retained earnings	**356,824**
Closing balance under IAS 39 (31 December 2017)	3,712,214
Transfer from statutory credit risk reserve	283,976
Recognition of expected credit losses for balances with banks	(508)
Recognition of expected credit losses for placements with other banks	(601)
Recognition of expected credit losses for other financial assets	(65,048)
Recognition of expected credit losses for off balance sheet	(9,928)
Recognition of expected credit losses for loans and advances	(283,976)
IFRS 15 day 1 adjustment for HF Development & Investments Limited	(169,283)
IFRS 15 day 1 adjustment for Kahawa Downs Limited	(31,508)
Related tax	158,803
Opening balance under IFRS 9 (1 January 2018)	**3,594,141**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(c) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Typically the Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of 60 days, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

Exposure to liquidity risk

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets are considered as including cash and cash equivalents and investment securities for which there is an active and liquid market less any deposits from financial institutions and commitments maturing within the next 91 days. Details of the reported Group ratio of net liquid assets to customers' deposits at the reporting date and during the reporting period were as follows:

	2018	2017
At 31 December	21.00%	20.70%
Average for the year	20.00%	21.38%
Maximum for the year	22.90%	28.72%
Minimum for the year	16.30%	14.18%

Contractual maturity analysis of financial assets and liabilities

The table below analyses the liquidity position of the Group's financial assets and liabilities:

31 December 2018:	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
Financial liabilities						
Customer deposits	4,627,586	16,115,988	4,950,150	129,881	10,278,662	36,102,267
Bank deposits	578,216	-	-	-	-	578,216
Loans from banks	258,450	606,235	1,677,285	4,746,131	1,943,778	9,231,879
Borrowings	-	-	2,294,596	-	-	2,294,596
Corporate bond	-	-	3,341,298	-	-	3,341,298
Government income notes	-	-	-	-	50,750	50,750
Total	**5,464,252**	**16,722,223**	**12,263,329**	**4,876,012**	**12,273,190**	**51,599,006**
Letters of credit	-	6,603	-	-	-	6,603
Guarantees	3,000	28,100	106,396	40,661	-	178,157
Unrecognised loan commitments	-	-	1,875,523	-	-	1,875,523
	3,000	**34,703**	**1,981,919**	**40,661**	**-**	**2,060,283**
At 31 December 2018	**5,467,252**	**16,756,926**	**14,245,248**	**4,916,673**	**12,273,190**	**53,659,289**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(c) Liquidity risk (continued)

Financial 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
Customer deposits	5,387,262	17,076,969	4,754,294	150,819	9,291,247	36,660,591
Bank deposits	83,682	-	-	-	-	83,682
Loans from banks	60,812	873,568	2,678,873	7,012,794	2,365,259	12,991,306
Corporate bond	-	-	-	3,047,369	-	3,047,369
Government income notes	-	-	-	-	50,750	50,750
Total	**5,531,756**	**17,950,537**	**7,433,167**	**10,210,982**	**11,707,256**	**52,833,698**
Guarantees	-		14,261	92,264	31,600	138,125
Letters of credit	142,127	-	-	-	-	142,127
Unrecognised loan commitments	-	1,889,776	3,053,218	-	-	4,942,994
	142,127	**1,889,776**	**3,067,479**	**92,264**	**31,600**	**5,223,246**
At 31 December 2017	**5,673,883**	**19,840,313**	**10,500,646**	**10,303,246**	**11,738,856**	**58,056,944**

Liquidity reserves

The following table sets out the components of the Group's liquidity reserves.

Liquidity reserves	Carrying/ Fair value Amount 2018 KShs'000	Carrying/ Fair value amount 2017 KShs'000
Cash at hand	356,884	447,263
Balances with Commercial Banks	137,373	808,624
Balances with Central Bank of Kenya:	2,423,468	2,823,460
Placements with other banks	1,904,995	1,492,637
Gorverment securities	3,212,140	2,287,296
Total liquidity reserves	**8,034,860**	**7,859,280**

(d) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(d) Market risk (continued)

(i) Foreign exchange risk

Foreign exchange risk arises from recognised assets and liabilities. The Group's exposure to foreign currency risk arose from assets denominated in US Dollars, EUR and GBP was as follows:

All figures are in Kenya shillings (KShs'000')

USD	2018	2017
Cash in bank	115,952	4,092,814
Loans and advances to customers	4,734,645	5,720,376
Borrowings	(6,768,580)	(8,956,599)
Net statement of financial position exposure	**(1,917,983)**	**856,591**

All figures are in Kenya shillings (KShs'000')

EUR	2018	2017
Cash in bank	22,372	14,286
Loans and advances to customers	30	-
Net statement of financial position exposure	**22,402**	**14,286**

All figures are in Kenya shillings (KShs'000')

GBP	2018	2017
Cash in bank	21,242	17,284
Loans and advances to customers	66,071	70,409
Net statement of financial position exposure	**87,313**	**87,693**

The following significant exchange rates applied during the period:

	Average rates 2018	Closing rates 2018
US Dollar	101.84	101.80
EUR	116.44	116.59
GBP	129.01	130.36

	Average rates 2017	Closing rates 2017
US Dollar	102.45	103.18
EUR	114.72	123.77
GBP	135.55	139.47

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(d) Market risk (continued)

(i) Foreign exchange risk (continued)

Sensitivity analysis on exchange rates

The Group is exposed to risk of loss arising from future potential adverse movements in exchange rates.

A 10 percent strengthening of the Kenya Shilling against the USD,EUR and GBP at 31 December 2018 would have increased the profit for the period after tax by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remains constant.

A 10 percent weakening of the Kenya Shilling against the USD,EUR and GBP at 31 December 2018 would have had the equal but opposite effect on the US Dollar balances to the amounts shown above, on the basis that all other variables remain constant.

	Profit or loss		Equity	
	Strengthening	**Weakening**	**Strengthening**	**Weakening**
31 December 2018				
USD 10% Movement	134,259	(134,259)	134,259	(134,259)
EUR 10% Movement	(1,568)	1,568	(1,568)	1,568
GBP 10% Movement	(6,112)	6,112	(6,112)	6,112
31 December 2017				
USD 10% Movement	(59,961)	59,961	(59,961)	59,961
EUR 10% Movement	(1,000)	1,000	(1,000)	1,000
GBP 10% Movement	(6,139)	6,139	(6,139)	6,139

(ii) Sensitivity analysis interest rate risk

At 31 December 2018, if interest rates at that date had been 100 basis points lower with all other variables held constant, pre-tax profit for the year would have been KShs 9.501 million (2017 – KShs 12.108 million) lower arising mainly as a result of lower interest income and other components of equity would have been KShs 6.651 million (2017 – KShs 8.475 million) lower arising mainly as a result of lower interest income loans and advances.

If interest rates had been 100 basis points higher, with all other variables held constant, pre-tax profits would have been KShs 9.501 million (2017 - KShs 12.108 million) higher, arising mainly as a result of higher interest income on loans and advances and other components of equity would have been KShs 6.651 million (2017 – KShs 8,475 million) higher, arising mainly as a result of higher interest income loans and advances.

(iii) Other price risk

The Group does not hold any financial instruments subject to price risk.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(e) 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 Board 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 the Group's independent risk control to ensure compliance with the Group's risk limits. The Group's risk limits are assessed regularly to ensure their appropriateness given the Group's objectives and strategies and current market conditions.

(f) Capital risk 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 Group to maintain a prescribed ratio of total risk weighted assets. This requirement is calculated for market risk in the banking portfolio of HFC Limited.

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 Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Group 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 Group and its individually regulated operations have complied with all externally imposed capital requirements throughout the year. There has been no material change in the Group's management of capital during the period.

The regulatory capital position for HFC Limited, the Group's banking subsidiary, as at 31 December 2018 was as follows:

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

4. FINANCIAL RISK MANAGEMENT (Continued)

(f) Capital risk management (continued)

	2018 KShs'000	2017 KShs'000
Tier 1 capital		
Ordinary share capital	5,000,000	5,000,000
Share premium	3,513,662	3,513,662
Retained earnings	(1,440,413)	600,656
Deferred tax	(147,479)	(816,436)
Total tier 1 capital	**6,925,770**	**8,297,882**
Tier 2 capital		
Regulatory reserve	611,754	640,800
Qualifying subordinated liabilities	73,115	170,602
Total tier 2 capital	**684,869**	**811,402**
Total regulatory capital	**7,610,639**	**9,109,284**
Risk weighted assets	**48,940,357**	**53,575,584**

Capital ratios	**2018**	**2017**
Total regulatory capital expressed as a percentage of total risk-weighted assets	15.55%	17.00%
Total tier 1 capital expressed as a Percentage of risk-weighted assets	14.15%	15.49%

Central Bank of Kenya required the Group to maintain a minimum core capital of KShs 1 billion as at 31 December 2018.

The Group is compliant with this requirement.

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Group may limit the amount of dividends paid to shareholders

5. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

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

(a) Critical accounting estimates and assumptions

(i) Allowances for credit losses

Assets accounted for at amortised cost are evaluated for impairment on a basis described in accounting policy 3(i).

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

5. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

(i) Allowances for credit losses (continued)

Judgement is made on classification of financial assets assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial assets are Solely for Payment of Principal and Interest (SPPT) on the principal amount outstanding.

Judgement is made in establishing the criterion for determining whether credit risk on the financial instrument has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of Expected Credit Losses (ECLs) and selection and approvals of models used to measure ECL.

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about counterparty's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and advances and held-to-maturity investment securities with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired loans and advances and held-to-maturity investment securities, but the individual impaired items cannot yet be identified. In assessing the need for collective loss allowances, management considers factors such as credit quality, portfolio size, concentrations and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The measurement of impairment losses both under IFRS 9 and IAS 39 across all categories of financial assets requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Group's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Group's debtors transition matrix model, which assigns PDs to debtors and other financial assets.
- The Group's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a ECL basis and the qualitative assessment.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

5. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

(a) Critical accounting estimates and assumptions (continued)

(i) Allowances for credit losses (continued)

— The segmentation of financial assets when their ECL is assessed on a collective basis

— Development of ECL models, including the various formulas and the choice of inputs

— Determination of associations between macroeconomic scenarios and, economic inputs, such as interest rates levels and collateral values, and the effect on PDs, EADs and LGDs

— Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models

(ii) Income taxes

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

(iii) Fair value of financial instruments

Where the fair values of the financial assets and finance liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable market data where possible, but where this is not feasible, a degree of judgment is required in establishing fair values.

(b) Critical judgements in applying the entity's accounting policies

In the process of applying the Group's accounting policies, management has made judgements in determining:

— The classification of joint arrangements;

— Assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are SPPI on the principal amount outstanding.

— The classification of financial assets;

— Lease classifications;

— Establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for ncorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL

— Depreciation rates for property and equipment.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

6. OPERATING SEGMENTS

Operating segments defined at HF Group Plc are organised in four main reporting segments. The segmentation is based on the Group's management and internal reporting structure.

The following summary describes the operations of each of the Group's reportable segment;

- **Retail banking:** This segment is mainly responsible for sourcing residential mortgages for individual owner occupiers, micro loans, personal loans and it forms the major proportion of the loan lending book of the Group. The segment is also responsible for the sourcing of deposits from retail customers which are then used to finance the Group's loan products.

- **Corporate banking:** This segment is responsible for sourcing for deposits from corporate organizations. It is also incharge of projects, providing lending to property developers for construction. This includes construction of residential houses for sale, construction of office blocks, schools, hospitals and other related infrastructure.

- **Property Development:** This function is undertaken by one of the Group's subsidiaries, HF Development and Investment Limited and its core business is the development of housing projects and the sale of houses thereof.

- **Bancassuarance:** The bancassurance function is based at the HF Insurance Agency Limited and the business is procuring insurance business and earning commissions thereof.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before income tax, as included in the internal management reports that are reviewed by the Group's executive committee.

Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of each.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

6. OPERATING SEGMENTS (Continued)

	Retail Banking		Corporate Banking		Property Development		Bancassurance		Totals	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Interest income	3,293,696	3,572,135	2,751,825	3,560,491	-	-	-	-	6,045,521	7,132,626
Interest expense:	(1,953,683)	(1,986,242)	(1,658,071)	(2,088,110)	-	-	-	-	(3,611,754)	(4,074,352)
Net interest income	**1,340,013**	**1,585,893**	**1,093,754**	**1,472,381**	-	-	-	-	**2,433,767**	**3,058,274**
Non interest income	273,435	257,768	29,442	26,089	846,394	886,181	55,117	54,938	1,204,388	1,224,976
Depreciation and amortisation	(226,863)	(205,175)	(138,843)	(144,280)	(15,692)	(568)	(241)	(205)	(381,639)	(350,228)
Reporting segment profit/ (loss) before income tax	(409,708)	51,990	14,429	340,976	(172,970)	(55,467)	15,936	16,946	(552,313)	354,445
Loan disbursements	1,981,915	3,552,540	987,175	3,581,340	-	-	-	-	2,969,090	7,133,880
Loan sales	296,263	777,394	1,489,340	2,566,288	-	-	-	-	1,785,603	3,343,682
Deposits balances	15,743,509	15,549,809	19,701,391	21,276,553	-	-	-	-	35,444,900	36,826,362
Other material non cash items										
Impairment losses on mortgage loans	(223,334)	(347,995)	(152,574)	(228,208)	-	-	-	-	(375,908)	(576,203)
Capital expenditure	139,525	1,601	4,445	1,684	2,677	-	725	-	147,372	3,285
Reportable segment assets	29,804,245	28,373,874	27,298,355	33,755,586	2,806,619	5,035,382	76,167	63,485	59,985,386	67,228,327
Reportable segment liabilities	**19,534,752**	**21,525,868**	**28,389,075**	**30,687,977**	**454,044**	**3,979,196**	**24,733**	**21,798**	**48,402,604**	**56,214,839**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

6. OPERATING SEGMENTS (Continued)

Reconciliations of reportable segment revenues, profit or loss, assets and liabilities

	2018 KShs'000	2017 KShs'000
Net interest income		
Total net interest income for reportable segments	2,433,767	3,058,274
Other interest income adjustments	(168,094)	(81,906)
Consolidated net interest income	**2,265,673**	**2,976,368**
Non interest income		
Total non interest income for reportable segments	1,204,388	1,224,976
Other non interest income	114,669	121,450
Consolidated non interest income	**1,319,057**	**1,346,426**
Profit or loss		
Total profit or loss for reportable segments	(552,313)	354,445
Other profit or loss	(90,431)	(42,821)
Consolidated profit before income tax	**(642,744)**	**311,624**
Assets		
Total assets for reportable segments	59,985,386	67,228,327
Other assets	563,964	312,789
Consolidated total assets	**60,549,350**	**67,541,116**
Liabilities		
Total liabilities for reportable segments	48,402,604	56,214,839
Other liabilities	1,775,515	(123,258)
Consolidated total liabilities	**50,178,119**	**56,091,581**

7. INTEREST INCOME AND INTEREST EXPENSE

Interest Income *Arising from:*	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2017 KShs'000
Loans and advances to customers	5,661,554	6,713,482	-	-
Financial assets carried at amortised cost (2017:Held to maturity)	194,807	333,059	-	-
Financial assets carried at FVOCI (2017:Available for sale)	189,160	86,085	605	1,448
	6,045,521	**7,132,626**	**605**	**1,448**

Included in interest income on loan and advances for the year is a total of KShs 969,798,658 (2017 – KShs 883,442,123) accrued interest on impaired assets.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

7. INTEREST INCOME AND INTEREST EXPENSE (Continued)

Interest expense	**Group 2018**	**Group 2017**	**Company 2018**	**Company 2017**
Arising from:	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Deposits from banks	126,790	110,940	-	-
Deposits from customers	2,173,142	2,323,445	-	-
Interest on borrowed funds	1,479,916	1,721,873	-	-
	3,779,848	**4,156,258**	**-**	**-**

8. NON INTEREST INCOME

Fees and Commission income	214,725	224,321	-	-
Trading Income	38,173	50,221	-	-
Rental Income	50,170	43,141	-	-
House sale Income	846,394	886,181	-	-
Other operating income	169,595	142,447	387,934	421,282
Gain on sale of equipment	-	115	-	-
	1,319,057	**1,346,426**	**387,934**	**421,282**

9. NON INTEREST EXPENSES

Arising from:	**Group 2018**	**Group 2017**	**Company 2018**	**Company 2018**
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**
Salaries and employee benefits	1,227,078	1,088,000	208,407	146,720
Rental expenses	155,526	110,467	-	-
Depreciation of property and equipment (Note 22)	181,033	167,792	142	53
Amortisation of intangible assets (Note 24)	200,105	182,398	-	-
Amortisation of operating lease (Note 23)	643	643	-	-
Deposit Protection Fund	52,573	54,703	-	-
Cost of sold houses	803,487	803,487	-	-
Marketing expenses	156,003	44,442	-	-
Information Technology expenses	388,054	363,975	-	-
Legal expenses	142,580	81,216	-	-
Office expense	292,001	175,970	-	-
General administration expenses	261,424	339,103	150,392	91,856
	3,860,507	**3,412,196**	**358,941**	**238,629**

The following items are included with salaries and employee benefits:

	Group 2018	**Group 2017**	**Company 2018**	**Company 2017**
	Kshs' 000	**Kshs' 000**	**Kshs' 000**	**Kshs' 000**
Compulsory social welfare contributions	3,356	1,268	15	14
Contributions to the defined contribution retirement scheme	74,879	80,550	4,267	5,896
Number of employess in the Group	368	403	3	6

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

10. LOSS/PROFIT BEFORE TAXATION

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

	Group 2018 Kshs' 000	Group 2017 Kshs' 000	Company 2018 Kshs' 000	Company 2017 Kshs' 000
Directors' remuneration:				
- Fees	8,423	8,775	6,708	5,668
- Expenses	7,904	7,100	-	-
- as executives	64,139	64,413	64,139	64,413
Auditors' remuneration	13,478	12,803	1,618	1,558
Amortisation of prepaid operating lease rentals	643	643	-	-
Amortisation of intangible assets	200,105	182,398	-	-
Depreciation	181,033	167,792	142	53
Gain on sale of property and equipment	-	115	-	-

11. TAXATION

(a) Income tax expense

	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2017 KShs'000
Current tax at 30%	20,665	289,980	73	428
Deferred tax movement (Note 25(a))	(58,149)	(111,432)	(11,978)	(16)
- Prior year deferred tax (under)/over provision (Note 25(a))	(7,042)	6,860	1	-
	(44,526)	**185,408**	**(11,904)**	**412**

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

	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2017 KShs'000
Accounting profit before taxation	(642,744)	311,443	29,598	184,101
Tax at the applicable tax rate of 30%	(192,823)	93,433	8,879	55,230
Prior year (under)/over provision of deferred tax	(7,042)	6,860	1	-
Tax effect of non-deductible costs and tax exempt income	155,339	85,115	(20,784)	(54,818)
	(44,526)	**185,408**	**(11,904)**	**412**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

11. TAXATION (Continued)

(b) Taxation recoverable/(payable)

	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2017 KShs'000
At 1 January	204,009	86,907	13,585	1,130
Prior year adjustment	54,266	-	-	(6)
Paid during the year	23,341	407,082	11,621	12,889
Charge for the year	(20,665)	(289,980)	(73)	(428)
Impact of initial application of IFRS 15	50,785	-	-	-
At 31 December	**311,736**	**204,009**	**25,133**	**13,585**
The following amounts are shown in the balance sheet:				
Taxation recoverable	**311,739**	**204,012**	**25,133**	**13,585**
Taxation payable	**(3)**	**(3)**	**-**	**-**

12. EARNINGS PER SHARE

Basic

Earnings per share is calculated based on the profit attributable to shareholders divided by the number of ordinary shares in issue in each year as follows:

	2018 KShs'000	2017 KShs'000
Net (loss)/profit for the year attributable to shareholders	**(598,218)**	**126,216**
Number of ordinary shares in issue (000's)	**384,614**	**349,597**
Weighted average number of ordinary shares	**367,135**	**349,597**
Basic earnings per share	**(1.56)**	**0.36**
Weighted earnings per share	**(1.63)**	**0.36**

13. DIVIDENDS

(a) Proposed dividends

Proposed dividends are accounted for as a separate component of equity until they have been ratified at an annual general meeting. A final dividend in respect of the year ended 31 December 2018 of KShs Nil per share (2017 - KShs 0.35) amounting to a total of KShs Nil (2017 - KShs 122,362,002) has been proposed. No interim dividend was paid during the year (2017 Nil). The total dividend for the year is therefore KShs Nil per share (2017 - KShs 0.35), amounting to a total of KShs Nil (2017 - KShs 122,362,002). Issued and fully paid ordinary shares were 384,614,168 as at 31 December 2018 (2017 – 349,536,667).

(b) Reconciliation of dividends payable

	2018 KShs'000	2017 KShs'000
As at 1 January 2018	49,058	60,755
Proposed dividends (prior year)	122,359	174,691
Transfer from retained earnings	3	46
Dividends paid during the year	(143,365)	(186,434)
Balance as at 31 December	**28,055**	**49,058**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

14. FINANCIAL ASSETS AND LIABILITIES

The table below sets out the Group's classification of each class of financial assets and liabilities, their amortised cost and their fair values including accrued interest:

Group

	Amortised cost KShs'000	FVOCI KShs'000
31 December 2018:		
Financial assets		
Cash and cash equivalents	2,917,725	-
Placements with banks	1,904,995	-
Investment in Government securities	515,801	2,696,339
Loan advances to banks	253,404	-
Loan advances to customers	43,186,287	-
	48,778,212	**2,696,339**

	Amortised cost KShs'000	FVOCI KShs'000
Financial liabilities		
Customer and Bank deposits	35,299,040	**-**
Corporate bond	3,051,811	**-**
Shareholders' income notes	50,750	
Borrowings	10,416,938	**-**
	48,818,539	**-**

31 December 2017:	Held to maturity KShs'000	Loans and receivables KShs'000	Amortised cost KShs'000	Available for Sale KShs'000
Financial assets				
Cash and cash equivalents	-	-	4,079,347	-
Placements with banks	-	-	1,492,637	-
Investment in Government securities	746,179	-	-	1,541,117
Loan advances to banks	-	270,953	-	-
Loan advances to customers	-	49,368,686	-	-
	746,179	**49,639,639**	**5,571,984**	**1,541,117**
Financial liabilities				
Customer and Bank deposits	-	-	36,744,273	-
Corporate bond	-	-	3,047,369	-
Shareholders' income notes and loans	-	-	50,750	
Borrowings	-	-	12,991,306	-
	-	**-**	**52,833,698**	**-**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

14. FINANCIAL ASSETS AND LIABILITIES (CONTINUED)

The fair value of treasury bonds is based on the indicative price of the specific issues as at the reporting date. The indicative prices are derived from Bloomberg. For Treasury bills, placements with other banks, cash and cash equivalents and deposits the amortised cost is deemed a reasonable approximation of fair value because of their short term nature.

The fair value of loan advances has not been disclosed as this cannot be determined reliably.

Valuation hierarchy

The valuation hierarchy, and types of instruments classified into each level within that hierarchy, is set out below:

	Level 1	Level 2	Level 3
Fair value determined using:	Unadjusted quoted prices in an active market for identical assets and liabilities	Valuation models with directly or indirectly market observable inputs	Valuation models using significant non-market observable inputs
Types of financial assets:	Actively traded government and other securities. Listed derivative instruments Listed equities	Corporate and other government bonds and loans Over-the-counter (OTC) derivatives	Corporate bonds in illiquid markets Highly structured OTC derivatives with unobservable parameters
Types of financial liabilities:	Listed derivative instruments.	Over-the-counter (OTC) derivatives	Highly structured OTC derivatives with unobservable parameters.

The table below shows the classification of financial instruments held at fair value by the level in the fair value hierarchy as at 31 December 2018:

31 December 2018:	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Total KShs'000
Financial assets				
Investment in government securities	3,212,140	-	-	3,212,140
Loans and advances to banks	-	253,404	-	253,404
Loans and advances to customers	-	43,186,287	-	43,186,287
	3,212,140	**43,439,691**	**-**	**46,651,831**
Financial liabilities				
Customer deposits	-	34,720,824	-	34,720,824
Deposits from banks	-	578,216	-	578,216
Corporate bond	-	3,051,811	-	3,051,811
Borrowings	-	10,416,938	-	10,416,938
	-	**48,767,789**	-	**48,767,789**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)
14. FINANCIAL ASSETS AND LIABILITIES (CONTINUED)

31 December 2017:	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Total KShs'000
Financial assets				
Investment in government securities	2,287,296	-	-	2,287,296
Loans and advances to banks	-	270,953	-	270,953
Loans and advances to customers	-	49,368,686	-	49,368,686
	2,287,296	**49,639,639**	**-**	**51,926,935**
Financial liabilities				
Customer deposits	-	36,660,581	-	36,660,581
Deposits from banks	-	83,692	-	83,692
Corporate bond	-	3,047,369	-	3,047,369
Borrowings	-	12,991,306	-	12,991,306
	-	**52,782,948**	**-**	**52,782,948**

15. CASH AND BALANCES WITH BANKS

	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2017 KShs'000
Cash at hand	356,884	447,263	-	-
Balances with commercial banks	137,373	808,625	34,167	28,384
Balances with Central Bank of Kenya:				
- Unrestricted	610,120	914,324	-	-
- Restricted (Cash Reserve Ratio)	1,813,348	1,909,135	-	-
Balance as at 31 December (Gross)	**2,917,725**	**4,079,347**	**34,167**	**28,384**
Cash at hand	356,884	447,263	-	-
Balances with commercial banks	137,373	808,625	34,167	28,384
Balances with Central Bank	2,423,468	2,823,459	-	-
	2,917,725	**4,079,347**	**34,167**	**28,384**
Less:Allowance for impairment losses	(642)	-	-	-
Balance as at 31 December (Net)	**2,917,083**	**4,079,347**	**34,167**	**28,384**

The Cash Reserve Ratio (CRR) is non-interest earning and is based on the value of deposits as adjusted for the Central Bank of Kenya requirements. At 31 December 2018, the Cash Reserve Ratio was 5.25% (2017 – 5.25%) of all deposits. These funds are available for use by the company in its day-to-day operations in a limited way provided that on any given day this balance does not fall below 3.00% requirement and provided that the overall average in the month is at least 5.25%.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

16. PLACEMENTS WITH OTHER BANKS

	Group 2018 KShs'000	Group 2017 KShs'000
Placements with commercial banks	**1,904,695**	**1,492,637**

The weighted average effective interest rate on placements with other banks was 3.50% (2017 – 9.99%).

Placements with other banks

	2018 KShs'000	2017 KShs'000
Placement with other Banks	1,904,995	1,492,637
Less: Allowance for impairment losses	(300)	-
	1,904,695	**1,492,637**

17. INVESTMENT IN GOVERNMENT SECURITIES

	Group 2018 KShs'000	Group 2017 KShs'000
Held at amortised cost		
Treasury bills and bonds due after 180 days	515,801	-
Held to maturity	-	746,179
FVOCI		
Treasury bonds held at FVOCI	2,696,339	-
Available for sale	-	1,541,117
	3,212,140	**2,287,296**
From HTM to amortised cost (low risk)	515,801	746,179
Less: Allowance for impairment losses- (Stage 1)	-	-
Balance as at 31 December	**515,801**	**746,179**
From available for sale to FVOCI (low risk)	2,696,339	1,541,117
Less: Allowance for impairment losses- (Stage 1)	-	-
Balance as at 31 December	**2,696,339**	**1,541,117**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

18. LOAN ADVANCES AT AMORTISED COST

	2018 KShs'000	2017 KShs'000
(a) Loan advances at amortised cost		
Loans and advances to banks (gross)	253,610	270,953
Less: Provision for impairment losses	(206)	-
Net loans and advances to banks	**253,404**	**270,953**
Loans and advances to customers (gross)	46,351,897	52,337,232
Less: Provision for impairment losses	(3,165,165)	(2,968,546)
Net loans and advances to customers	**43,186,732**	**49,368,686**
Maturing:		
Within five years	14,634,711	15,967,839
Over five years to ten years	13,569,191	12,399,813
Over ten years to fifteen years	13,106,015	16,202,384
Over fifteen years	5,295,590	8,038,149
Gross loans and advances at amortised cost	**46,605,507**	**52,608,185**

(b) Loss allowance on financial instruments

The following table provides a reconciliation between:

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

	Loans and advances to banks at amortised cost	Loans and advances to customers at amortised cost	Guarantees and letters of credit cost	Cash and cash equivalents	Other financial assets and receivable	Total
Net re-measurement of loss allowance	9	389,758	1,176	134	1,304	392,381
Financial assets derecognized	-	(15,530)	(642)	(301)	-	(16,473)
	9	**374,228**	**534**	**(167)**	**1,304**	**375,908**

Impairment	Impairment losses	Portfolio impairment	Total
2017:	**KShs'000**	**KShs'000**	**KShs'000**
Impairment made in the period	1,098,622	-	1,098,622
Provisions no longer required	(521,067)	(1,352)	(522,419)
At 31 December 2017	**577,555**	**(1,352)**	**576,203**

The weighted average effective interest rate on loan advances to customers as at 31 December 2018 was 10.72% (2017 – 11.84%)

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

19. INVESTMENT IN SUBSIDIARIES AND JOINT VENTURES

(a) Subsidiaries	Shareholding	Company 2018 KShs'000	Company 2017 KShs'000
HFC Limited	100%	8,513,662	8,513,662
HF Development and Investment Limited	100%	1,440,000	1,440,000
First Permanent (East Africa) Limited	100%	5,020	5,020
HF Insurance Agency Limited	100%	100	100
		9,958,782	**9,958,782**

(b) Joint ventures

		Group 2018	Group 2017
Kahawa Downs Limited	50%	128,297	168,208
Precious Heights Limited	50%	94,775	106,289
Richland Development Limited	50%	164,943	167,752
Claycity Limited	33%	488,219	489,472
Theta Dam Estate Limited	50%	805,035	805,035
		1,681,269	**1,736,756**
Group share of profit/(loss) in joint venture			
Kahawa Downs Limited	50%	16,440	(8,403)
Precious Heights Limited	50%	(2,885)	(11,515)
Richland Development Limited	50%	(6,066)	(2,809)
Claycity Limited	33%	1,574	(44)
Theta Dam Estate Limited	50%	(122)	-
		8,941	**(22,771)**
Net investment in joint venture		**1,690,210**	**1,713,985**

The Group has entered into the following joint ventures for development of housing units in Kahawa Wendani, Riruta, Ruiru, Thika Road in Nairobi and Kamiti Road in Kiambu:

(b) Joint ventures (continued)

- Kahawa Downs Limited;
- Precious Heights Limited;
- Richland Development Limited;
- Claycity Limited and
- Theta Dam Estate Limited

The entities are jointly controlled with each party holding 50% of the shareholding in all joint ventures except in Claycity Limited, where the Group holds a 33% shareholidng. The Group contributed capital which is equivalent to value of the land where the housing units are being developed. They are structured as a separate vehicle and the Group has a residual interest in their net assets. Accordingly, the Group has classified its interest in these entities as a joint venture, which is equity accounted.

The following are summarized financial information for Kahawa Downs Limited, Precious Heights Limited, Richland Development Limited and Claycity Limited based on their financial statements prepared in accordance with IFRS. There were no revenue and expenses in the profit or loss for Theta Dam Estate Limited during the year.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

19. INVESTMENT IN SUBSIDIARIES AND JOINT VENTURES (Continued)

(b) Joint ventures (continued)

Group 2018:	Kahawa Development Limited KShs'000	Precious Heights Limited KShs'000	Richland Development Limited KShs'000	Claycity Limited KShs'000	Theta Dam Estate Limited KShs'000	Total KShs'000
Revenue	241,685	350	1,206	12,987	-	**256,228**
Operating costs	(211,808)	(8,593)	(12,976)	(4,320)	(244)	**(237,941)**
Income tax expense	3,003	2,473	(362)	(3,896)	-	**1,218**
Profit/(loss) and other comprehensive income	**32,880**	**(5,770)**	**(12,132)**	**4,771**	**(244)**	**19,505**
Group share of net profit/ (loss) (50%)	**16,440**	**(2,885)**	**(6,066)**	**1,574**	**(122)**	**8,941**
Current assets	441,997	636,523	1,723,789	1,575,979	1,950,000	**6,328,288**
Current liabilities	(100,278)	(129,811)	(709,451)	(101,995)	-	**(1,041,535)**
Net assets	**341,719**	**506,712**	**1,014,338**	**1,473,984**	**1,950,000**	**5,286,753**
Groups share of net assets	**170,860**	**253,356**	**507,169**	**486,415**	**975,000**	**2,392,799**
Group's interest in net assets at the beginning of the year	159,805	94,776	164,943	489,428	805,035	**1,713,987**
IFRS 15 Adjustment	(31,508)	-	-	-	-	**(31,508)**
Additions during the year	-	-	-	(1,210)	-	**(1,210)**
Closing Group Interest	**128,297**	**94,776**	**164,943**	**488,218**	**805,035**	**1,681,269**
Share of total comprehensive income	**16,440**	**(2,885)**	**(6,066)**	**1,574**	**(122)**	**8,941**
Carrying amount of interest in investee at end of the year	**144,737**	**91,891**	**158,877**	**489,792**	**804,913**	**1,690,210**

2017:	Kahawa Development Limited KShs'000	Precious Heights Limited KShs'000	Richland Development Limited KShs'000	Claycity Limited KShs'000	Theta Dam Estate Limited KShs'000	Total KShs'000
Revenue	114,660	23,535	-	563	-	**138,758**
Operating costs	(146,250)	(52,389)	(5,617)	(651)	-	**(204,907)**
Income tax expense	14,784	5,824	-	-	-	**20,608**
Profit/(loss) and other Comprehensive income	**(16,806)**	**(23,030)**	**(5,617)**	**(88)**	**-**	**(45,543)**
Group share of net profit/ (loss) (50%)	**(8,403)**	**(11,515)**	**(2,809)**	**(44)**	**-**	**(22,771)**
Current assets	557,611	291,286	644,768	1,506,313	1,913,117	**4,913,095**
Current liabilities	(238,001)	(101,736)	(316,384)	(36,930)	-	**(693,051)**
Net assets	319,610	189,550	328,384	1,469,383	1,913,117	**4,220,045**
Groups share of net assets (50%)	159,805	94,775	164,192	734,691	956,559	**2,110,022**
Group's interest in net assets at the beginning of the year	168,208	106,289	167,752	32,826	805,035	**1,280,110**
Additions during the year	-	-	-	456,646	-	**456,646**
Closing Group Interest	**168,208**	**106,289**	**167,752**	**489,472**	**805,035**	**1,736,756**
Share of total comprehensive income	(8,403)	(11,515)	(2,809)	(44)	-	**(22,771)**
Carrying amount of interest in investee at end of the year	**159,805**	**94,774**	**164,943**	**489,428**	**805,035**	**1,713,985**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

20. OTHER ASSETS

	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2018 KShs'000
Staff debtors	-	136,621	-	-
Prepayments	239,145	259,979	500	727
Deposits and rent receivable	51,845	51,599	-	-
House sales debtors	11,034	434,414	-	-
Other receivables	109,387	605,195	96,613	53,815
	411,411	**1,487,808**	**97,113**	**54,542**

21. HOUSING DEVELOPMENT PROJECTS

	2018 KShs'000	2017 KShs'000
Group:		
Housing projects		
Housing Projects	**2,537,972**	**2,414,469**

There were no commitments in respect of these projects authorized in 2018 (2017 - Nil).

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

22. PROPERTY AND EQUIPMENT

(a) Group 2018:	**Freehold land**	**Buildings**	**Furniture, fixtures, equipment & motor vehicles**	**Work in progress**	**Total**
Cost or valuation:	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
At 1 January 2018	62,000	805,184	1,266,893	3,284	2,137,361
Additions	-	-	11,975	-	11,975
Disposals	-	-	(3,728)	-	(3,728)
Transfer from Investment Property	-	748,548	-	-	748,548
Transfers	-	-	3,284	(3,284)	-
Revaluation	-	-	860	-	860
Impairment	-	-	(47,154)	-	(47,154)
At 31 December 2018	**62,000**	**1,553,732**	**1,232,130**	**-**	**2,847,862**
Comprising:					
At cost	10,000	769,199	1,231,270	-	2,010,469
At valuation	52,000	784,533	860	-	837,393
	62,000	**1,553,732**	**1,232,130**	**-**	**2,847,862**
Depreciation:					
At 1 January 2018	-	36,013	583,968	-	619,981
Charge for the year	-	27,533	153,500	-	181,033
Disposals	-	-	(3,428)	-	(3,428)
Impairment	-	-	(28,702)	-	(28,702)
At 31 December 2018	**-**	**63,546**	**705,338**	**-**	**768,884**
Carrying amounts:					
At 31 December 2018	**62,000**	**1,490,186**	**526,792**	**-**	**2,078,978**

Group 2017:	**Freehold land**	**Buildings**	**Furniture, fixtures, equipment & motor vehicles**	**Work in progress**	**Total**
Cost or valuation:	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
At 1 January 2017	52,000	655,184	1,217,598	14,652	1,939,434
Additions	-	-	37,593	577	38,170
Disposals	-	-	(243)	-	(243)
Transfers	-	-	11,945	(11,945)	-
Revaluation	10,000	150,000	-	-	160,000
At 31 December 2017	**62,000**	**805,184**	**1,266,893**	**3,284**	**2,137,361**
Comprising:					
At cost	-	20,651	1,266,893	3,284	1,290,828
At valuation	62,000	784,533	-	-	846,533
	62,000	**805,184**	**1,266,893**	**3,284**	**2,137,361**
Depreciation:					
At 1 January 2017	-	54,968	426,379	-	481,347
Charge for the year	-	10,077	157,714	-	167,791
Disposals	-	-	(125)	-	(125)
Revaluation	-	(29,032)	-	-	(29,032)
At 31 December 2017	**-**	**36,013**	**583,968**	**-**	**619,982**
Carrying amounts:					
At 31 December 2017	**62,000**	**769,171**	**682,925**	**3,284**	**1,517,380**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

22. PROPERTY AND EQUIPMENT (Continued)

(a) Group (continued

The land and buildings, were revalued on 31 December 2017 by Tysons Limited, a firm of independent professional valuers on the basis of open market value for existing use.The resulting surplus was credited to revaluation reserve. The motor vehicle was revalued at 860,000 during the year after being fully depreciated while still in use.

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

	2018	2017
	KShs 000	KShs '000
Freehold land	206	206
Buildings	3,211	3,624

Included in equipment are assets with a gross value of KShs 275,504,322 (2017 - KShs 187,958,382) which are fully depreciated and still in use. Such assets would have attracted a notional depreciation of KShs 55,100,864 (2017 - KShs 33,215,996). Revaluation of the Group's assets is done after every 3 years.

(b) Company

2018:	Furniture, fixtures, equipment & motor vehicles KShs'000	Total KShs'000
Cost or valuation:		
At 1 January 2018	657	657
Additions	265	265
At 31 December 2018	**922**	**922**
Depreciation:		
At 1 January 2018	85	85
Charge for the year	142	142
At 31 December 2018	**227**	**227**
Carrying amounts:		
At 31 December 2018	**695**	**695**
2017:		
Cost or valuation:		
At 1 January 2017	277	-
Additions	380	-
At 31 December 2017	**657**	**-**
Depreciation:		
At 1 January 2017	32	32
Charge for the year	53	53
At 31 December 2017	**85**	**85**
Carrying amounts:		
At 31 December 2017	**572**	**572**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

23. PREPAID OPERATING LEASE RENTALS

	Group 2018 KShs'000	Group 2017 KShs'000
Cost:		
At 1 January and 31 December	54,612	54,612
Additions	-	-
At 31 December 2018	**54,612**	**54,612**
Amortisation:		
At 1 January	10,504	9,861
Charge for the year	643	643
Prior year under provision	181	-
As at 31 December	**11,328**	**10,504**
Carrying amounts At 31 December	**43,284**	**44,108**

As at 31 December 2018 the un-expired lease period ranges from 58 to 84 years. Leasehold land is recognised at cost. The Group's leasehold land was valued professionally on 31 December 2017 at KShs 512,000,000.

24. INTANGIBLE ASSETS

	Group 2018 KShs'000	Group 2017 KShs'000
Cost:		
At January	1,590,571	1,548,411
Additions during the year	135,397	42,160
Reclassification	(127)	-
As at 31 December	**1,725,841**	**1,590,571**
Amortisation:		
At January	518,183	335,786
Amortisation during the year	200,105	182,398
As at 31 December	**718,228**	**518,184**
Carrying amounts:		
As at 31 December	**1,007,553**	**1,072,387**

Included in the intangible assets is the Group's banking subsidiary, HFC Limited, Core Banking Software amounting to KShs 1,294,905,015 that was rolled out on 1 January 2016, whose estimated useful life is 8 years.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)
25. DEFERRED TAX ASSETS/(LIABILITIES)

Recognised deferred tax assets and liabilities are attributable to the following:

(a) Group

2018:	**01.01.2018**	**Tax impact on initial application of IFRS 9**	**Recognized in profit or loss**	**FVOCI**	**Prior Year**	**31.12.2018**
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Arising from:						
Property and equipment	(114,905)	-	(70,338)	-	1,468	(183,775)
Revaluation surplus	(46,376)	-	(2,903)	-	2,903	(46,376)
Financial assets at FVOCI	20,250	-	-	(18,114)	-	2,136
Other general provisions	5,738	5,256	9,824	-	238	21,056
Unrealised exchange losses	1	-	-	-	-	1
Trading losses	75,234	-	128,827	-	-	204,061
General provision on loans and advances	899,557	102,762	(7,261)	-	2,433	997,491
Net deferred tax	**839,499**	**108,018**	**58,149**	**(18,114)**	**7,042**	**994,594**

2017:	**01.01.2017**	**Prior year under provision**	**Recognized in profit or loss**	**Recognized in other compre-hensive income**	**31.12.2017**
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Arising from:					
Property and equipment	(21,379)	(9,419)	(84,107)	-	(114,905)
Revaluation surplus	(36,924)	-	-	(9,452)	(46,376)
AFS Fair value reserves	32,106	-	-	(11,856)	20,250
Other general provisions	9,960	-	(4,222)	-	5,738
Unrealised exchange losses	(63)	-	64	-	1
Trading Losses	-	2,559	72,675	-	75,234
General provision on mortgages and advances	772,535	-	127,022	-	899,557
Net deferred tax	**756,235**	**(6,860)**	**111,432**	**(21,308)**	**839,499**

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

25. DEFERRED TAX ASSETS/(LIABILITIES) (Continued)

(b) Company

2018:	**01.01.2018**	**Tax impact on initial application of IFRS 9**	**Recognized in profit or loss**	**31.12.2018**
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**
Property and equipment	(31)	-	(13)	(44)
Trading losses	53	-	(53)	-
General provisions	-	3,854	12,044	15,898
Net deferred tax	**22**	**3,854**	**11,978**	**15,854**

The deferred taxation asset has not been recognised in these financial statements due to uncertainty of the timing when sufficient future taxable profits to realise the asset will be realised. This position will be reviewed at subsequent reporting dates.

2017:	**At 01.01.2017**	**Recognized in profit or loss**	**31.12.2017**
	KShs'000	**KShs'000**	**KShs'000**
Arising from:			
Property and equipment	(4)	(27)	(31)
Trading losses	10	43	53
Net deferred tax	**6**	**16**	**22**

26. EMPLOYEE BENEFITS

Employee Share Ownership Plan (ESOP)

Movement in the number of share options held for the employees under the Employee Share Ownership Plan is as follows:

	2018 Number of shares	**2017 Number of shares**
Outstanding at start of year	775,000	485,000
Granted during the year	-	845,000
Lapsed	(655,000)	(400,000)
Exercised ESOP during the year	(120,000)	(155,000)
Outstanding at end of year	**-**	**775,000**
Exercise price per share – KShs	**10.00**	**10.00**

Options may be exercised at the price of KShs 10. The trading price of HF Group PLC share as at 31 December 2018 on the Nairobi Securities Exchange was KShs 5.54 (2017 – KShs 9.25). All Nil (2017 – 775,000) outstanding shares were exercised as at 31 December 2018.

Back ground of Employee Share Ownership Plan

On 26 July 2006, the shareholders gave approval for an Employee Share Ownership Plan (ESOP) to be set up to facilitate the ownership of shares in HF Group PLC by employees of the company. Approval to issue additional shares, listing of shares and allotment to the Employee Share Ownership Plan (ESOP) was approved by Capital Market Authority on 20 December 2010. The total number of shares approved under the ESOP amount to 5,750,000.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2017 (CONTINUED)

26. EMPLOYEE BENEFITS (Continued)

The ESOP is for Group employees (excluding non-executive board Directors) who have attained the age of 18 years, have completed the probationary period and have been confirmed as employees of the Group in accordance with their contract of employment. However, the right to exercise an Option shall terminate immediately upon the option holder ceasing to be an eligible employee, unless the holder of an unexercised option dies before exercising a subsisting option, where the option may be exercised by his personal representatives within 12 months of the date of death. The eligible employees pay for the units by cash at a price determined by Trustees either in full or by instalments until price is paid in full. The unit holder is not allowed to sell, transfer or otherwise dispose of units registered in his name to another unit holder or to any third party whatsoever. The administrative offices of the ESOP – Unit Trust are the Principal Offices of the Company..

27. CUSTOMERS' DEPOSITS

	Group 2018	Group 2017
	KShs'000	KShs'000
Government and parastals:		
Payable within 90 days	1,864,895	1,635,542
Payable after 90 days and within one year	385,697	-
Payable after one year	3,976,784	3,926,996
Private sector and individuals:		
Payable within 90 days	18,580,849	26,123,909
Payable after 90 days and within one year	4,217,751	4,754,294
Payable after one year	5,694,848	219,850
	34,720,824	**36,660,591**

Included in customer deposits are deposits due to related parties listed in note 40

28. DEPOSITS FROM BANKS

	Group 2018	Group 2017
	KShs'000	KShs'000
Money market deposits	578,216	83,682

29. OTHER LIABILITIES

	Group 2018 KShs'000	Group 2017 KShs'000	Company 2018 KShs'000	Company 2018 KShs'000
Interest payable on the Government of Kenya income notes	2,107	2,093	-	-
House sales deposits	263,460	124,118	-	-
Withholding tax payable	116,001	59,690	-	-
Sundry creditors	39,871	61,993	-	-
Trade creditors	233,170	131,125	-	-
Insurance Premium payable	330,674	52,391	-	-
Short term borrowing	-	1,047,636	-	-
Deferred expenses	91,872	1,013,326	-	-
Other liabilities	305,117	767,200	251,422	111,156
	1,382,272	**3,259,572**	**251,422**	**111,156**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

30. INVESTMENT PROPERTY

	2018 KShs'000	2017 KShs'000
As at 1 January	748,549	-
Additions during the year	-	748,549
Transfer to property and equipment (note 22)	(748,549)	-
As at 31 December	-	**748,549**

Investment property comprises a commercial property that is leased to third parties. Each of the leases contains an initial non-cancellable period, with annual rents indexed to consumer prices. No contigent rents are charged. During the year 2018, the investment property was transferred to property and equipment as a result of its intended use having changed from property for sale to internal use by the Group.

The investment property was independently valued by Tyson's Limited as at 31 December 2017. The valuer is registered and licensed by the Valuers Registration Board of Kenya and has the relevant experience and knowledge of valuing the various properties in the portfolio. The property was valued at KShs 1,100,000,000.

31. LOANS AND BORROWINGS

(a) Borrowings from banks and financial institutions	Group 2018 KShs'000	Group 2017 KShs'000
European Investment Bank (EIB)	3,285,478	3,783,468
Ghana International Bank (plc)	510,212	1,550,554
Norwegian Investment Fund for Developing Countries	628,935	880,474
Shelter Afrique	931,670	1,063,131
International Finance Corporation	-	591,099
Symbiotics SA	1,344,901	1,813,752
East African Development Bank	1,018,205	1,032,215
NIC Bank Ltd	516,250	517,307
Arab Bank for Economic Development in Africa	233,502	-
Cooperative Bank Kenya Ltd	-	309,643
	8,469,153	**11,541,643**

During the year, the Group, through the banking subsidiary HFC Limited, received USD 2.25 million from Arab Bank for Economic Development in Africa (BADEA) at an interest rate of 6 months Libor plus a margin of 5% for 10 years.

In 2017, the Group, through the banking subsidiary HFC Limited received USD 22 million from EIB at an interest rate of 4.321% for 7 years,USD 15 million from Ghana International Bank at a rate of 3 months Libor plus a margin of 5% for 2 years and two short term notes from NIC Bank Limited KShs 500 million and Co-operative Bank of Kenya Limited KShs 300 million at a rate of 14% and 13% respectively for one year. The Cooperative Bank facility was repaid in 2018 while the NIC Bank facility was renewed for another one year.

In 2015, HF Group Limited received three tranches from European Investment Bank of USD 7,088,000 at a rate of 5.037%, KShs 356,283,794 at a rate 10.664% and KShs 447,052,320 at a rate of 10.712% while in 2012 the Company received two loan tranches from European Investment Bank of KShs 668,085,425 at 10.783 % and KShs 211,000,000 at 11.269%.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

31. LOANS AND BORROWINGS (Continued)

(a) Borrowings from banks and financial institutions (continued)

All the tranches are for a period of 7 years for lending to Small and Medium Enterprises in the real estate sector. Interest and principal are payable semi-annually with a 2 year grace period for principal repayments. In 2014, the Group received KShs 1 billion from Norfund at an interest rate of the weighted average rate of the 182 Treasury bill auction immediately preceeding the interest payment date plus a margin of 3% . The facility is for 7 years with interest and principal being paid semi – annually. A USD 20 million loan was received from International Finance Corporation on 1 July 2013. The loan is for 5 years at a rate of 6 months USD Libor plus a margin of 4.30%.

Interest is paid half-yearly with a 2 year grace period on the principal loan repayment and this facility was fully repaid in 2018. In 2015, the company received a loan of USD 10 million from Shelter Afrique for a period of 10 years with effect from 23 December 2015 at the rate of 6 months USD Libor plus a margin of 6.35%. Interest is paid half-yearly with a 2 year grace period on the principal loan repayment. In 2016, the company received USD 10 million from East African Development Bank for 7 years with effect from 20 December 2016 at a rate of 7.25%. Interest is paid semi-annually.

During the year, the company did not default on any of the loan repayment obligations from all the existing lenders.

(b) Borrowed funds

	2018	2017
	KShs'000	KShs'000
Group:		
Cresent Finco LLP	1,493,741	739,233
Shelter Afrique	454,044	710,430
	1,947,785	**1,449,663**

The loan from Crescent Finco LLP drawn as at 1 January 2018 is KShs 739,233,472. An additional 754,507,806 was drawn during the year. The loan is secured with a first legal charge over the project on Title Number Nairobi/Block 156/1. The loan balance as at 31 December 2018 was Kshs 1,493,741,278 at an effective rate of 18.5%.

In 2015, HF Development and Investment Limited (formerly Kenya Building Society Ltd (KBSL) which is a 100% owned subsidiary of HF Group Ltd entered into a financing arrangement with Shelter Afrique for development of housing units at Komarock Estate. The facility is secured by the land where the development is taking place. The loan is at Shelter Afrique's base rate currently at 18.7%. Both interest and principal are payable on a quarterly basis. The loan balance as at 31 December was KShs 454,044,155.

(c) Reconciliation of the movement in Loans and Borrowings:

	2018	2017
	KShs'000	KShs'000
At 1 January	12,991,306	9,518,705
Funds Received	952,156	5,377,085
Payments on principal and interest	(3,526,524)	(1,904,484)
Net Movement in Borrowings	(2,574,368)	3,472,601
At December	**10,416,938**	**12,991,306**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

32. CORPORATE BOND

	2018 KShs'000	2017 KShs'000
Opening balance	3,047,369	10,217,910
Interest accrual	394,536	874,899
Payments on principal and interest	(390,094)	(8,045,440)
Net movement in corporate bond	4,442	(7,170,541)
Closing balance	**3,051,811**	**3,047,369**

In 2010, the Group raised KShs 7,030,900,000 under the 7 year MTN whose programme size is KShs 10,000,000,000.

In 2012, the Group raised KShs 2,969,100,000 which was the balance on the 7 year KShs 10 billion Medium Term Note (MTN) programme. The total amount is at a fixed rate of 13%. The term note is payable in on 14 October 2019.

The total notes on a fixed rate of 8.5% per annum amount to KShs 5,865,400,000 while the total notes on floating rate are KShs 1,165,500,000. The floating rate notes were on a margin of 3% plus 182 day Treasury bill rate of the last auction immediately preceding the interest payment date subject to a minimum of 5% per annum and maximum of 9.5% per annum.The first tranche of KShs 7,030,900,000 was successfully redeemed on 2 October 2017 while the second tranche of KShs 2,969,100,000 shall be redeemed on 14 October 2019.

33. CAPITAL AND RESERVES

Group and Company:

	2018	2017
(a) Ordinary share capital Authorised:	**KShs'000**	**KShs'000**
At 1 January		
500,000,000 (2017 – 500,000,000) ordinary shares		
of KShs 5.00 each	2,500,000	2,500,000
2018 – Nil (2017 – Nil) additional shares		
of KShs 5.00 each authorized during the year	-	-
At 31 December		
500,000,000 (2017 – 500,000,000) ordinary		
Shares of KShs 5.00 each	**2,500,000**	**2,500,000**

(b) Ordinary share capital

Issued and fully paid:		
At 1 January:		
349,536,667 (2017 – 349,381,667) ordinary shares		
of KShs 5.00 each	1,747,683	1,746,908
34,957,501 (2017 – Nil) Bonus shares of		
Kshs 5.00 each	174,788	-
120,000 (2017 – 155,000) ordinary		
shares of KShs 5.00 each issued in the year	600	775
At 31 December		
384,614,168 (2017 – 349,536,667)		
ordinary shares of KShs 5.00 each	**1,923,071**	**1,747,683**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

33. CAPITAL AND RESERVES (Continued)

(b) Ordinary share capital issued and fully paid (continued)

The holders of ordinary shares rank equally with regard to the Company's residual assets, are entitled to receive dividends declared from time to time and are entitled to one vote per share at general meetings of the company. Issued and fully paid ordinary shares were 384,614,168 as at 31 December 2018 (2017 – 349,536,667). During the year, 120,000 (2017 - 155,000) shares were issued under employee share ownership program at KShs 10 per share leading to a share premium of KShs 5 (2017 – KShs 5) per share.

(c) Share premium

This reserve arises when the shares of the company are issued at a price higher than the nominal (Par) value.

(d) Revaluation reserve

The revaluation reserves include the net change in the fair value of land, buildings, motor vehicle, furniture and equipment and are to be held until the property is derecognised.

	2018	2017
	KShs'000	KShs'000
As at 1 January	179,580	-
Change in fair value during the period:		
Land and builidings	-	189,032
Motor vehicle	860	-
Less: Related tax	-	(9,452)
As at 31 December	**180,440**	**179,580**

(e) Regulatory reserve

The regulatory reserve represents an appropriation from retained earnings to comply with the Prudential Guidelines of the Central Bank of Kenya on loan loss provisions. The balance represents the excess of impairment provisions determined in accordance with the

Prudential Guidelines over the impairment provisions recognised in accordance with the

International Financial Reporting Standards. The reserve is non-distributable.

The opening balance of regulatory reserve has been reduced by KShs 284m relating to the increase in credit loss allowance on initial application of IFRS 9.

(f) Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of investments and treasury bonds held at FVOCI (2017- available for sale) until the investment is derecognised when the net changes are recycled to profit or loss.

	2018	2017
	KShs'000	KShs'000
As at 1 January	(48,226)	(75,890)
Change in fair value during the year:		
Treasury bonds classified as		
FVOCI (2017 available for sale)	60,379	39,520
Less: Related tax	(18,114)	(11,856)
As at 31 December	**(5,961)**	**(48,226)**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

34. SHAREHOLDERS' INCOME NOTES AND LOANS

	2018 KShs'000	2017 KShs'000
Government of Kenya – Income Notes	**50,750**	**50,750**

The Government of Kenya – Income Notes carry no redemption date and are charged interest at a fixed rate of 8.25% per annum (2017 – 8.25%).

35. NOTES TO THE STATEMENT OF CASH FLOWS

(a) Group reconciliation of operating profit to net cash flows from operating activities

	2018 KShs'000	2017 KShs'000
Profit before taxation	(642,744)	311,624
Adjustments for:		
Depreciation	181,033	167,792
Amortisation of intangible assets	200,105	182,398
Amortisation of prepaid operating lease rentals	643	643
Profit on sale of property and equipment	(89)	115
Decrease of balances with Central Bank of		
Kenya – Cash Reserve Ratio (CRR)	95,787	257,525
Decrease in customer and banks deposits	(1,445,233)	(1,962,753)
Decrease in loans and advances to customers	5,915,972	4,829,966
Investment in Government securities	(864,465)	1,837,774
Increase in Investment properties	-	(748,549)
Increase in housing projects	(123,503)	(414,165)
Profit on investment in joint ventures	(8,941)	22,771
Decrease in other assets	817,924	16,679
Increase in other liabilities	(1,898,762)	1,123,096
Increase in other liabilities	(1,836,559)	1,123,096
Net cash flows from operating activities before tax	**2,227,727**	**5,624,916**
Income tax paid	(23,341)	(407,082)
Net cash flows from operating activities	**2,204,386**	**5,217,834**

(b) Analyses of cash and cash equivalents (including restricted balances)

	2018 KShs'000	2017 KShs'000	Change in the year KShs'000
Cash in hand and bank	1,104,377	2,170,212	(1,065,835)
Balances due from banking institutions	1,904,995	1,492,637	412,358
	3,009,372	**3,662,849**	**(653,477)**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

35. NOTES TO THE STATEMENT OF CASH FLOWS (Continued)

(c) Company reconciliation of operating profit to net cash flows from operating activities

	2018	2017
	KShs'000	KShs'000
Profit before taxation	29,598	184,101
Depreciation	142	53
Increase in other assets	(10,172)	(26,716)
Increase in other liabilities	140,266	1,267
Net cash flows from operating activities before tax	**159,834**	**158,705**
Income tax paid	(11,621)	(12,889)
Net cash flows from operating activities	**148,213**	**145,816**

(b) Company analyses of cash and cash equivalents

	2018 KShs'000	2017 KShs'000	Change in the year KShs'000
Cash in hand and bank	**34,167**	**28,384**	**5,783**

36. CONTINGENT LIABILITIES

(a) Guarantees

As at 31 December 2018, the company had issued guarantees and letters of credit in the ordinary course of business to third parties as shown below.

	2018	2017
	KShs'000	KShs'000
Guarantees	178,157	138,125
Letters of credit	6,603	142,127
	184,760	**280,252**

(b) Other contingent liabilities

In the ordinary course of business, the Group and its subsidiaries are defendants in various litigations and claims. Although there can be no assurances, the Directors believe, based on the information currently available and legal advice, that the claims can successfully be defended and therefore no provision has been made in the financial statements. The significant claims are described below:

ICEA LION Group (ICEA) has sued HFC Limited, a subsidiary of HF Group Plc, and others for loss of KShs 120m which were funds withdrawn by the third defendant, ICEA's former Assistant General Manager, and deposited with Nyaga Stock Brokers. The Company's advocates have filed a defence against ICEA.

Sharok Kher Mohamed sued HFC Limited, a subsidiary of HF Group Plc, for selling the property by public auction in 2000. The plaintiff was awarded judgment for KShs 20 million plus interest. HFC Limited have appealed against the judgment and the matter is pending in the Court of Appeal. Directors believes that the defence against the action will be successful.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

37. OPERATING LEASE ARRANGEMENTS

The bank as a lessor

Rental income earned during the year was KShs 50,170,164 (2017 – KShs 43,141,397). At the reporting date, the Group had contracted with tenants for the following future lease receivables:

	2018	2017
	KShs'000	**KShs'000**
Within one year	45,191	41,601
In second to fifth year inclusive	121,768	134,138
After five years	652	1,558
	167,611	**177,297**

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 Group as a lessee

Rental expenses incurred during the year were KShs 155,525,780 (2017 – KShs 110,466,634). At the reporting date, the Group had outstanding commitments under operating leases which fall due as follows::

	2018	2017
	KShs'000	**KShs'000**
Within one year	99,294	82,242
In second to fifth year inclusive	172,666	176,963
After five years	-	-
	271,960	**259,205**

Operating lease payments represent rentals payable by HFC Group PLC for its branch premises. Leases are negotiated for an average term of 6 years.

38. MORTGAGE COMMITMENTS

Group:

Loan commitments amounting to KShs 1,875,523,000 (2017 – KShs 4,942,993,944) are analysed below:

	2018	2017
	KShs'000	**KShs'000**
Commitment in principle but not authorised for payment	1,575,411	1,889,776
Authorised but not paid	300,112	3,053,218
	1,875,523	**4,942,994**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018 (CONTINUED)

39. CAPITAL COMMITMENTS

Group:		
Authorised but not contracted	-	53,740

40. ASSETS PLEDGED AS SECURITY

As at 31 December 2018, there were no assets pledged by the Group to secure liabilities nor secured Group liabilities other than as disclosed on Note 31.

41. RELATED PARTY TRANSACTIONS

Group:

(a) Loans

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

	2018	2017
	KShs'000	KShs'000
At 1 January	1,024,499	1,095,525
Loans advanced during the year	188,249	312,389
Loans repayments received	(339,063)	(383,415)
At 31 December	**873,685**	**1,024,499**
Comprising:		
Mortgages and advances	733,826	888,970
Personal loans	124,022	121,988
Staff car loans	15,837	13,541
At 31 December	**873,685**	**1,024,499**

Included in related party are staff car loans of KShs 15,837,090 (2017 – KShs 13,540,721) and staff personal loans of KShs 124,058,827 (2017 – KShs 121,988,266). The related interest income for staff car loans and staff personal loans in 2018 was KShs 1,523,649 (2017 – KShs 1,473,863) and KShs 9,831,995 (2017 – KShs 8,658,112) respectively.

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 10.

(c) Compensation to senior management including executive directors for the year ended 31 December 2018 amounted to KShs 227,105,141 (2017 – KShs 243,172,012).

	2018	2017
(d) Transactions with Britam Insurance Company (Kenya) Limited		
	KShs'000	KShs'000
Bank balances held with HFC Limited	163,152	224,267
(e) Transactions with Britam Assets Managers Limited		
Bank balances held with HFC Limited	1,500,000	700,000

PROXY FORM

To The Registrar

HF Group PLC

Rehani House

Kenyatta Avenue

P.O. Box 30088

00100 Nairobi GPO

I/We ____

Of ____

Being a member/members of HF Group Plc hereby appoint ______________________

____

of ____

or failing him, the duly appointed Chairman of the meeting to be my/our proxy to vote for me/us on my/our behalf at the 53rd Annual **General Meeting** of the Company to be held on the 26th day of April 2019, or at any adjournment thereof.

Number of shares held ____

Account number: ____ (if known)

Signed this ______________________ day of ______________________ 2019.

Signed

____

Note:

1. In case of a member being a corporation, the proxy must be under the Common Seal or under the hand of an officer or attorney duly authorised.
2. The proxy form should be completed and returned to the Registrar by 11.00 AM on 24th April 2019, failing which it will be invalid.

FOMU YA UWAKILISHI

KWA: The Registrar

HF Group PLC

Rehani House

Kenyatta Avenue

S.L.P 30088-00100

NAIROBI

Mimi/ Sisi: ____

Kutoka: ____

Kama mwanachama wa HF GROUP Plc namteua: ______________________________

____

Kutoka ____

Au akikosa, mwenyekiti wa mkutano kuwa wakala wangu/ wetu kupiga kura kwa niaba yangu/yetu wakati wa kikako cha mkutano wa 53 wa pamoja wa mwaka wa kampuni utakaofanyika Aprili 26, 2019 au kuahirishwa.

Idadi ya hisa zinazomilikiwa ______________________________

Nambari ya akaunti: ______________________________ (endapo inajulikana)

Imetiwa sahihi ______________ tarehe ______________________ 2019.

Sahihi

____

Muhimu:

1. Endapo mwanachama atakuwa shirika, fomu ya uwakilishi iwe imepigwa mhuri rasmi au kutiwa sahihi na afisa au mwanasheria aliyeidhinishwa kikamilifu
2. Fomu ya uwakilishi ijazwe na kurejeshwa kwa Msajili kabla ya Saa Tano Asubuhi Aprili 24, 2019 na endapo itachelewa, haitakuwa na umuhimu wowote.

HF Group
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Toll Free: 0800 721 400
Email: housing@hfgroup.co.ke
Website: www.hfgroup.co.ke

HF GROUP
Dreams Made Possible