Contents:

Directors

Back row left to right: Sachit Shah, B Rogers, S S Shah (Executive Director).
Front row left to right: S B R Shah (Chairman), M J Karanja.

Directors, Officers and Administration

DIRECTORS

S B R Shah	(Chairman - Appointed 23 March 2004)
P J Ransley	(Chairman - Resigned 31 December 2003)
S S Shah	(Executive Director)
B Rogers	
M J Karanja	
S Shah	

SECRETARY

N P Kothari – FCPS (Kenya)

AUDITORS

KPMG Kenya
16th Floor, Lonrho House
PO Box 40612
00100 – Nairobi

REGISTERED OFFICE

I&M Bank House
2nd Ngong Avenue
P O Box 30238
00100 – Nairobi

BRANCHES

I&M Bank House
2nd Ngong Avenue
PO Box 30238
00100 – Nairobi

I&M Bank Tower
Kenyatta Avenue
PO Box 30238
00100 – Nairobi

Sarit Centre
Westlands
PO Box 30238
00100 – Nairobi

Jethalal Chambers
Biashara Street
PO Box 30831
00100 – Nairobi

Biashara Bank Building
Nyerere Avenue
PO Box 86357
80100 – Mombasa

Changamwe Road
Industrial Area
PO Box 17601
00500 – Nairobi

Tivoli Centre
Court Road
PO Box 424
40100 - Kisumu

MAJOR CORRESPONDENT BANKS

ABN Amro Bank NV
ABSA Bank
American Express Bank Limited
Standard Bank of South Africa
CitiBank, NA
Natexis Bank

Dresdner Bank AG, Frankfurt
Habib Bank AG Zurich, Zurich
HDFC Bank
ICICI Bank
Indus Ind Bank

Chairman's Statement

S B R Shah

It gives me great pleasure in presenting to you the Annual report and financial statements of your Bank of the year ended 31st December 2003.

For the last 10 years, we have had the pleasure of having Justice P J Ransley as our Chairman, who had to relinquish his position on his elevation to the Bench. My fellow Directors join me in extending our grateful thanks to Justice Ransley for his guidance and strong support as the Chairman through the formative years of the Bank.

THE ECONOMY - 2003

After the historic victory of the National Rainbow Alliance Coalition (NARC) headed by His Excellency, President Kibaki, there was great excitement that the country was going to witness historic changes. The private sector reacted very positively, encouraged by the election manifesto of NARC and the encouragement from the new Government. The Kenyan economy steadied itself, albeit the growth rate remained low, because of various reasons. Undoubtedly, the task facing the young Government was not easy and expectations from every quarter were very high. The promise to provide a clean Government was received well internationally. It was a great relief to hear that our development partners decided to come to our rescue and assist us in rebuilding our country.

BANKING SECTOR

For the banking industry, the gradual reduction in the interest rates was a welcome development. Moneys tied up with Central Bank of Kenya in treasury bills started trickling back to the banking sector and most of the Banks were flushed with deposits which improved liquidity. While demand for credit picked up, new products were also introduced and the customer suddenly had an array of loan products to choose from, such as housing loans, personal loans, car loans, education loans etc. Competition also provided variety, choice and better pricing coupled with quality service.

The Kenyan economy steadied itself, albeit the growth rate remained low, because of various reasons. Undoubtedly, the task facing the young Government was not easy and expectations from every quarter were very high

The low interest rate policy and the 'clean up' at the Judiciary, had a beneficial impact on the recovery of non-performing assets, which had brought the industry to its knees. The year, therefore, witnessed a sharp transformation in the performance of most banks, and this has restored the confidence in the local banking industry.

Chairman's Statement

continued

However there are some serious issues which have to be considered to ensure that the banking industry can expand and play a more meaningful role in economic development.

1. Security has deteriorated considerably and it is hoped that the serious efforts of the Government in revamping the police force will bring about substantial improvement. Costs of security features in bank premises such as cameras, bullet proof glass, electronic surveillance equipment, guards etc have pushed costs too high, thus affecting the viability of smaller branches. This has also hampered the enthusiasm of commercial banks in increasing branch network and reaching out to the rural and semi-urban areas.

2. Documentation procedure for securing loan facilities is becoming more and more cumbersome and time consuming. Not only are there delays but there is also more risk of impairment of legal documentation held. Many of the Acts concerning our industry need to be reviewed to simplify procedures and reduce costs, which will benefit our customers.

3. Communication is critical to our industry as branches are networked. Banking is becoming more dependent on information technology and frequent interruptions cause delays and make our operations inefficient. Delicate equipment is damaged when there are power surges. Most banks have had to install costly generators and large uninterrupted power supply (UPS) units to ensure seamless operations.

4. Manpower Costs. There have been regular increases in remuneration of unionisable staff without commensurate increase in productivity, which has steadily pushed up costs. We are now a high 'wage island' and the restructuring we have seen in the industry is a direct result of such unaffordable increases. Wages in other industries for similar work have to have some correlation.

5. Bank charges have been much discussed in the media. It is pertinent to point out that the variance in such charges from bank to bank clearly demonstrate that there is a wide choice available to the customers. Random criticism is unfair to those banks which are efficiently run, with reasonable charges and superior levels of service. Even the interest rate spreads have reduced to the extent that has never been witnessed in Kenya before.

6. Banking is becoming a highly capital intensive industry requiring heavy investment in equipment. Our depreciation charge for the year was enormous, amounting to Kshs. 45 Million. Technological obsolescence has resulted in increased capital expenditure on Information Technology, both hardware and software. Software is subject to multiple taxation by way of reverse withholding tax and VAT which increases the cost of software in Kenya and delays the introduction of latest technology into the country.

BANK'S PERFORMANCE

The merger of Biashara Bank of Kenya with I&M Bank, through an acquisition of assets and liabilities as at 1st January 2003 has created a much stronger entity. Some of the noteworthy achievements as per the audited accounts are highlighted below:

			(Shs. 000s)
	2002	**2003**	**Increase %**
No of branches	3	7	133
Shareholders equity	1,137,678	1,696,081	49
Customer deposits	5,364,071	10,142,230	89
Total assets	7,176,411	12,130,025	69

The success of the merger can be attributed to the meticulous planning which went into this project involving our management staff at various levels. Any such major corporate restructuring brings about serious challenges, which we were fully prepared for. It must be acknowledged that our customers were very understanding and made very useful suggestions for which we are most thankful.

The strengths of the merger have brought about the following benefits:

1. The peak exposure limit or the maximum amount that the Bank can lend to a group, increased to Kshs. 400 million approx.

2. The operational efficiency or non-interest expenses to gross operating income reduced from 57% to 50%.
3. The level of non-performing assets (net of provisions and suspended interest) against total gross advances reduced from 12.4% to 5.65%.

The Bank is now better geared to face competition and make further improvements in 2004.

OUTLOOK FOR THE BANK

We have always believed in looking ahead as we have confidence in the country. This is amply borne out by our decision to invest in I&M Bank Tower, in 1997, when most investors were reducing exposure to Kenya. We have successfully managed to let out 11 floors to the East African Standard Group and KTN. This is probably the single largest letting in the history of Kenya

We will continue to invest in IT and communication technology. Since the beginning of the year, we have already launched our SMS banking and Infomail products which were developed in house. These products are offered as additional features to our products and there is no charge for this service.

Very soon we shall be launching our call centre, which will reduce the time taken to respond to customer's queries. In order to keep customers updated, we are launching smart statements, wherein statements can be sent by fax automatically, without any manual intervention.

In order to automate our document archival system, the Bank has also invested in OMNIDOCS, a state of art system for safe-keeping Banks records and documents.

The Bank has also been examining the possibility of expanding its existing network of 7 branches and considering a presence in the neighbouring countries.
Our branch network has resulted in an increase in retail customers and it will be our endeavor to offer more products specifically to cater to this important sector of our business. We have already started issuing ATM Cards, which can be used at any Kenswitch ATM. There has been a remarkable improvement in the usage of ATMs and with the expansion of the network during the year, we hope to see better acceptability.

CORPORATE SOCIAL RESPONSIBILITY

The Bank has adopted the following bench marks for taking up social causes:-

1. Encouraging education of gifted children from financially handicapped backgrounds.
2. Supporting institutions which are providing shelter to orphaned children.
3. Feeding programmes.

Our primary aim to is involve our staff members in such programmes to develop social awareness at all levels.

A HISTORY OF PROFESSIONALISM

This is the 25th year of our operations as a financial institution. The original license was granted in May 1980 by His Excellency, President Mwai Kibaki, when he was the then Finance Minister. We can look back with satisfaction in the development of quality human resources. We have a full fledged human resources department which is responsible for addressing specific training needs, maintaining a cordial working atmosphere and ensuring that rewards are based purely on merit and performance. Not surprisingly, some of our former colleagues are spread all over the world working with banks, insurance companies and even the UN headquarters in New York.

CORPORATE GOVERNANCE

The Bank's board comprises 5 members of which one is executive. The non-executive directors have experience in diverse fields and are independent as far as day to day operations of the Bank are concerned. The Board has met four times during the year in discharge of its responsibilities and overall supervision of the Bank.

The Board Audit Committee (BAC) is chaired by Mr Brian Rogers. Apart from the Chairman of the Committee, the BAC has two non-Executive Directors as well as the Executive Director.

Various committees such as Credit Committee, Assets and Liabilities Committee, Management Committee, Human Resources Committee, Operations and IT Committees have met regularly for the proper functioning of the Bank. It is noteworthy that all branches and departments hold regular meetings to bring about improvements in professional management.

Chairman's Statement
continued

COMPLIANCE

The world is becoming a smaller place and the financial services industry needs to remain extra vigilant to deny criminals a safe haven for money laundering. Your Bank remains fully compliant in 'Know Your Customer' requirements and has conducted compulsory training for all members of staff to ensure that our country does not become a conduit for dirty money. It is our hope that all banks and forex bureaus will exercise caution in dealing with foreign currency remittances so that the industry is respected outside Kenya. In turn, the authorities should ensure a level playing field where all licensed players follow the same set of rules and regulations.

APPRECIATION

On behalf of my colleagues on the Board, I am pleased with the excellent team work of all our staff at various units and maintaining the high standards of the I&M Bank family. Thank you.

A very special thank you goes to our customers for giving us the opportunity to serve them and further strengthening our relationship which we cherish.

While we compete with each other, we do interact closely with member banks in coordinating our efforts in constant improvement in industry standards. We do acknowledge the valuable support from the Central Bank of Kenya (CBK), Kenya Bankers Association and our colleagues in the industry for the support, guidance and the privilege of working together. The enlarged local foreign currency cheques clearing arrangement would not have been possible without a joint effort. We also look forward to the success of the various initiatives by CBK such as the 'Real Time Gross Settlements' (RTGS) and other projects.

Our correspondent banks all over the world have given us excellent support. We are very thankful to all of them for providing us with adequate trade finance lines and efficient services at all times.

I would also like to record our appreciation to Mr. Claude Perio, the Chief Executive of PROPARCO, who paid us a visit in February 2004 inspite of his busy schedule. PROPARCO's line will help us in extending medium term loans in foreign currency for the creation of new capacities in various sectors.

As Chairman of the Board, I wish to thank my Board members for their support and guidance.

S B R Shah
Chairman of the Board

I&M News

French financing line for I&M Bank Ltd.

The French Financing Agency PROPARCO (Societe de Promotion et de Participation pour la Cooperation Economique) has extended a major US Dollar 4 million credit line to I&M Bank. This will in turn enable I&M Bank to offer long term US Dollar project financing at competitive rates to companies seeking to make investments in Kenya.

Senior officials of I&M Bank and PROPARCO sign a credit agreement

I&M Bank launches ATMs

During the year, I&M Bank launched its ATM services as members of the nationwide Kenswitch ATM network. This service has been very well received by customers and usage has been growing exponentially.

Kenswitch ATMs located at I&M Bank Tower

Report of the Directors

for the year ended 31 December 2003

The directors have pleasure in submitting their report together with the audited financial statements for the year ended 31 December 2003.

1. ACTIVITIES

The Bank provides an extensive range of Banking, financial and related services permitted under the Banking Act (Cap. 488).

2. SHARE CAPITAL

The Bank increased its authorised capital from KShs 750,000,000 to KShs 1,000,000,000 by the creation of 2,500,000 Ordinary Shares of KShs 100 each.

3. ACQUISITION

The transfer of assets to and assumption of liabilities of Biashara Bank of Kenya Limited by the Bank was effected from 24 hours (midnight) 31 December 2002 for a consideration of KShs 410,000,000/-. The amount of the consideration amounting to KShs 408,325,000 was paid by the issue of 2,500,000 Ordinary Shares of KShs 100/- in the capital of the company credited as fully paid to Biashara Bank of Kenya Limited and an amount of KShs 1,675,000 was paid in cash. The issued share capital of the Bank is KShs 1 billion with effect from 1 January 2003.

4. RESULTS

	KShs'000
Profit before taxation	284,833
Taxation	(89,755)
Profit after taxation	195,078
Proposed dividend	(100,000)
Retained profit for the year	**95,078**

5. DIVIDEND

The directors recommend the payment of a dividend of KShs 100 Million (2002 – KShs 45 Million).

6. DIRECTORS

The directors who served during the year and up to the date of this report are set out on page 3.

7. AUDITORS

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

8. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved at a meeting of the directors held on 23 March 2004.

BY ORDER OF THE BOARD

N P Kothari
Secretary

Date: 23 March 2004

Statement of Directors' Responsibilities

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

The directors accept responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act. The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the company and of its operating results. The directors further accept responsibility for the maintenance of accounting records, which may be relied upon in the preparation of financial statements, as well as adequate systems of internal financial control.

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

Director: S B R Shah

Director: M J Karanja

Director: S S Shah

Date: 23 March 2004

Report of the Independent Auditors

to the members of Investments & Mortgages Bank Limited

KPMG Kenya
Certified Public Accountants

Mail Address
P O Box 40612
00100 Nairobi GPO
Kenya

Office address
16th Floor, Lonrho House
Standard Street
Nairobi
Kenya

Telephone 254-20-222862
Fax: 254-20-215695
Email: info@kpmg.co.ke
Website: www.kpmg.co.ke

We have audited the financial statements set out on pages 12 to 40 for the year ended 31 December 2003. We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purposes of our audit. The financial statements are in agreement with the books of account.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND INDEPENDENT AUDITORS

As stated on page 10, the directors are responsible for the preparation of financial statements that give a true and fair view of the state of affairs of the company and its operating results. Our responsibility is to express an opinion on the financial statements based on our audit.

BASIS OF OPINION

We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting policies used and significant estimates made by the directors, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion, proper books of account have been kept and the financial statements give a true and fair view of the state of the company's financial position at 31 December 2003 and of its operating results and cash flows for the year then ended and comply with International Financial Reporting Standards and the Kenyan Companies Act.

KPMG Kenya

Date: 23 March 2004

Profit and loss account

for the year ended 31 December 2003

	Note	2003 KShs	2002 Restated KShs
Interest income	4	921,111,094	653,121,554
Interest expense	5	(295,838,995)	(330,816,118)
Net interest income		**625,272,099**	**322,305,436**
Impairment losses on loans and advances (net of recoveries)	15(b)	(120,516,541)	(74,423,593)
Net interest income after provision for impairment losses on loans and advances		**504,755,558**	**247,881,843**
Non interest income	6	183,508,784	103,993,196
Non interest expenses	7	(403,430,900)	(243,109,119)
Profit before taxation	8	**284,833,442**	**108,765,920**
Taxation	9	(89,755,348)	(48,999,962)
Profit after taxation		**195,078,094**	**59,765,958**
Earnings per share	10	**19.50**	**7.97**
Diluted earnings per share	10	**19.50**	**5.98**
Dividend per share	11	**10.00**	**6.00**

The notes set out on pages 16 to 40 form an integral part of these financial statements.

Balance Sheet
at 31 December 2003

	Note	2003 KShs	2002 KShs
ASSETS			
Cash and balances with Central Bank of Kenya	12	780,643,014	559,535,396
Investments in Government Securities	13	4,186,912,828	1,344,271,316
Placements with other Banks	14	450,364,993	595,397,081
Loans and advances to customers	15(a)	5,315,430,574	3,350,774,570
Other investments	16	117,067,833	104,101,209
Other assets	17	152,193,104	134,659,569
Equity investment	18	-	499,995
Goodwill	19	11,723,999	-
Deferred tax	20	21,692,929	3,743,882
Property and equipment	21	124,095,996	123,888,895
Investment property	22	855,276,945	843,608,012
Prepaid operating lease rentals	23	114,622,505	115,931,208
TOTAL ASSETS		**12,130,024,720**	**7,176,411,133**
LIABILITIES			
Deposits from other Banks and Banking institutions	24	114,266,270	607,377,812
Customer deposits	25	10,142,230,423	5,364,070,828
Taxation payable		32,230,108	10,053,389
Other liabilities	26	145,217,266	57,231,545
		10,433,944,067	6,038,733,574
SHAREHOLDERS' EQUITY (Page 15)			
Share capital	27	1,000,000,000	750,000,000
Share premium	28	158,325,000	-
Reserves		437,755,653	342,677,559
Dividend proposed		100,000,000	45,000,000
		1,696,080,653	1,137,677,559
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**12,130,024,720**	**7,176,411,133**

The financial statements set on page 12 to 40 were approved by the Board of Directors on 23 March 2004 and were signed on its behalf by:

Director: S B R Shah

Director: S S Shah

Director: M J Karanja

Secretary: N P Kothari

The notes set out on pages 16 to 40 form an integral part of these financial statements.

Cash flow statement

for the year ended 31 December 2003

	Note	2003 KShs	2002 KShs
Net cashflows from operating activities	29(a)	**(10,646,921)**	**(243,953,265)**
Cashflows from investing activities			
Acquisition of Biashara Bank of Kenya Limited, net of cash and cash equivalents acquired.	3	916,019,062	-
Disposal/(acquisition) of equity investments		499,995	(499,995)
Purchase of property and equipment		(27,142,656)	(14,298,596)
Purchase of investment property		(11,668,933)	(6,269,114)
Proceeds from disposal of property and equipment		188,542	236,441
Net cash utilised in investing activities		877,896,010	(20,831,264)
Cashflows from financing activities			
Dividend paid		(45,000,000)	(40,000,000)
Net cash utilised in financing activities		(45,000,000)	(40,000,000)
Net increase/(decrease) in cash and cash equivalents	29(b)	**822,249,089**	**(304,784,529)**

The notes set out on pages 16 to 40 form an integral part of these financial statements.

Statement of changes in equity

for the year ended 31 December 2003

	Share capital KShs	Share premium KShs	Retained earnings KShs	Proposed dividends KShs	Total KShs
At 31 December 2001	750,000,000	-	327,911,601	40,000,000	1,117,911,601
Net profit after taxation	-	-	59,765,958	-	59,765,958
Dividend proposed	-	-	(45,000,000)	45,000,000	-
Dividend paid	-	-	-	(40,000,000)	(40,000,000)
At 31 December 2002	**750,000,000**	**-**	**342,677,559**	**45,000,000**	**1,137,677,559**
Share capital issued	250,000,000	158,325,000	-	-	408,325,000
Net profit after taxation	-	-	195,078,094	-	195,078,094
Dividend proposed	-	-	(100,000,000)	100,000,000	-
Dividend paid	-	-	-	(45,000,000)	(45,000,000)
At 31 December 2003	**1,000,000,000**	**158,325,000**	**437,755,653**	**100,000,000**	**1,696,080,653**

The notes set out on pages 16 to 40 form an integral part of these financial statements.

Notes to the financial statements

for the year ended 31 December 2003

1 SIGNIFICANT ACCOUNTING POLICIES

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

(a) Basis of preparation

The financial statements are prepared in accordance with and comply with International Financial Reporting Standards.

The financial statements are prepared on a fair value basis for investment property, certain items of property and equipment and financial assets and liabilities held for trading. All other assets and liabilities are stated at either amortised cost or historical cost.

(b) Revenue recognition

(i) Net interest income

Interest income and expense is recognised in the income statement as it accrues, taking into account the effective yield of the asset. Interest income and expense includes the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

When loans become doubtful of collection, they are impaired to their recoverable amounts and interest income is thereafter recognised based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

(ii) Fee and commission income

Fee and commission income is recognised when the corresponding service is provided.

(iii) Rental income

Rental income from investment property is recognised in the profit and loss account on a straight-line basis over the term of the lease.

(c) Financial instruments

(i) Classification

A financial instrument is a contract that gives rise to both a financial asset of one enterprise and a financial liability of another enterprise. Financial instruments held by the Bank include balances with Central Bank of Kenya, loans and advances, investments in government securities, balances with Banks, deposits and derivative financial instruments.

Financial instruments are classified as follows:

Trading instruments are those that the Bank principally holds for the purpose of short-term profit taking. These include derivative instruments as described in Note 30.

Originated loans and receivables are loans and receivables created by the Bank providing money to a customer.

Held-to-maturity assets are financial assets with fixed or determinable payments and fixed maturity that the Bank has the intent and ability to hold to maturity.
Available-for-sale assets are financial assets that are not held for trading purposes, originated by the Bank, or held to maturity. Available-for-sale instruments include cash and balances with Central Bank of Kenya.

Financial liabilities are classified either as trading financial liabilities or other financial liabilities.

Other financial liabilities include customer deposits and deposits from Banking institutions.

(ii) Measurement

Financial instruments are measured initially at cost, including transaction costs.

Subsequent to initial recognition, all trading instruments and all available-for-sale assets are measured at fair value, except that any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses.

All non-trading financial liabilities, originated loans and receivables and held-to-maturity assets are measured at amortised cost less impairment losses. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Gains and losses arising from a change in the fair value of available-for-sale assets and trading instruments are recognised in equity and the profit and loss account respectively.

(d) Investments in Government Securities

(i) Treasury Bills

Treasury bills are classified as originated loans & receivables and carried at amortised cost.

(ii) Treasury Bonds - acquired directly from the Central Bank of Kenya

Treasury bonds acquired directly from the Central Bank of Kenya are classified as originated loans & receivables and carried at amortised cost. Amortised cost is the amount at which the bond was measured at initial recognition plus the cumulative interest earned thereon, less principal and interest payments received as well as any write-down for impairment.

(iii) Treasury Bonds - acquired from the secondary market

Treasury bonds acquired from the secondary market are classified as held-to-maturity financial instruments and carried at amortised cost. These are treasury bonds that the Bank has both the intent and ability to hold to maturity.

In all instances, amortised cost is calculated using the effective interest rate method.

(e) Other investments

Other investments are classified as held-to-maturity financial instruments. The Bank has both the intent and ability to hold these instruments to maturity.

(f) Loans and advances

Loans and advances originated by the Bank by providing money directly to a borrower are classified as originated loans and receivables and carried at amortised cost. Amortised cost is the amount at which the advance was measured at initial recognition plus the cumulative interest earned thereon, less principal and interest repayments as well as any write-down for impairment.

Loans are generally shown at the principal amount adjusted for any provision for impairment losses in order to reflect the estimated recoverable amounts.

(g) Impairment losses on loans and advances

Impairment losses are established if there is objective evidence that the Bank will not be able to collect all amounts due according to the original contractual terms of the loan. The amount of the provision is the difference between the carrying amount and the estimated recoverable amount. The estimated recoverable amount is the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate of the advance. If an advance has a variable interest rate, the discount rate for measuring recoverable amount is the current effective interest rate determined under the contract.

In addition, a general provision for impairment losses is maintained based on management's evaluation of the loans and advances portfolio and other exposures in respect of losses, which, although not specifically identified, are known from previous experience and the credit rating of the borrowers to be inherent in such a portfolio.

Increases/(decreases) in the provision for loan impairment losses are charged/(credited) to the income statement.

When an advance is deemed to be uncollectible, it is written off against the related provision for impairment losses. Subsequent recoveries are credited to the provision for impairment losses in the income statement.

(h) Derivative financial instruments

The Bank uses financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operational, financing and investment activities.

Derivative financial instruments are recognised initially at cost. Subsequent to initial recognition, derivative financial instruments are stated at fair value.

The fair value of forward exchange contracts is the amount of the mark to market adjustment at the balance sheet date.

(i) Transactions in foreign currencies

Transactions in foreign currencies during the year are converted into Kenya Shillings at the exchange rate ruling at the date of the transaction. Foreign currency monetary assets and liabilities are translated at the exchange rate ruling at the balance sheet date other than the forwards contracts which are carried at prevailing foward rates. Resulting exchange differences are recognised in the income statement for the year. Non monetary assets and liabilities denominated in foreign currency are recorded at the exchange rate ruling at the transaction date.

(j) Cash and cash equivalents

For the purpose of presentation in the cash flow statement, the cash and cash equivalents include balances with the Central Bank of Kenya which are available to finance the Bank's day to day operations, net balances from Banking institutions, and short term treasury bills.

(k) Taxation

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

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

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

(l) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of Bank's share of the net assets of the acquired company at the date of acquisition.

Amortisation is charged to the income statement on a straight-line basis over the estimated useful life of goodwill. Goodwill is amortised from the date of initial recognition. The estimated useful life of goodwill in respect of the acquisition of net assets of Biashara Bank of Kenya Limited is 4 years.

(m) Operating leases

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 are charged to the profit and loss account on a straight-line basis over the period of the lease.

(n) Property and equipment

Items of property and equipment are stated at historical cost less accumulated depreciation.

Depreciation is charged on a straight line basis at rates calculated to write down the cost of each asset, to its residual value over its estimated useful life as follows: -

- Leasehold improvements - Over the period of lease
- Computer equipment and computer software - 33 1/3 %
- Furniture, fittings & fixtures - 5% - 12½%
- Motor vehicles - 25%

Gains or losses on disposal of property, plant and equipment are determined by reference to their carrying amount and are taken into account in determining the operating profit.

(o) Investment property

Investment property is stated at fair value based on directors' valuation. Fair value is based on replacement cost for similar properties in the same location and condition. Any gain or loss arising from a change in fair value is recognised in the profit and loss account. Rental income from investment property is accounted for as described in accounting policy 1(b).

(p) Impairment of assets

The carrying amounts of the Bank's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If such indication exists, the assets recoverable amount is estimated and an impairment loss recognised whenever the carrying amount of an asset exceeds its recoverable amount.

The recoverable amount of the Bank's investments in held-to-maturity securities and receivables is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset. Receivables with a short duration are not discounted.

The recoverable amount of other assets is the greater of their net selling price and value in use. 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.

(q) Employee benefits

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

The assets of the defined contribution scheme are held in a separate trustee administered guarantees scheme managed by an insurance company. Retirement plans are funded by contributions from the employees and the Bank. The Bank's contributions are charged to the profit and loss account in the year to which they relate.

The employees and the Bank also contribute to the National Social Security Fund. Contributions are determined by local statute and the Bank's contributions are charged to the profit and loss account in the year to which they relate.

(r) Related party transactions

In the normal course of business, transactions have been entered with certain related parties. These transactions are at arms length.

(s) Dividends

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

2 THE CENTRAL BANK OF KENYA (AMENDMENT) ACT 2000

The Central Bank of Kenya (Amendment) Act, 2000 received assent on 6th August 2001. Subsequent to that date the Kenya Bankers Association filed a constitutional application at the High Court of Kenya. The Court delivered its verdict on 24th January 2002.

A Decree to confirm the Judgement was extracted on 22nd February 2002 and subsequently the Attorney General filed an application to have the Decree varied. A Consent Order to vary the Decree was granted, but was then challenged by the Central Bank of Kenya and the Kenya Bankers Association. The matter has not been determined to date and as such the Act continues to be inoperative.

The directors, based on the legal advice from the Bank's lawyers have interpreted this to mean that the Central Bank of Kenya (Amendment) Act 2000 may be ultra vires the Constitution of Kenya. The financial statements have been prepared accordingly.

3 ACQUISITION OF ASSETS AND LIABILITIES OF BIASHARA BANK OF KENYA LIMITED

On 1 January 2003, the Bank acquired Biashara Bank of Kenya Limited for a purchase consideration of Kshs 410,000,000. The transaction was accounted for using the purchase method.

Effect of acquisition

The purchase had the following effect on the Bank's assets and liabilities:

	2003 KShs
Assets	
Cash and balances with Central Bank of Kenya	282,234,350
Investments in Government Securities	1,291,923,511
Placements with other Banks	192,623,935
Other investments	7,168,917
Loans and advances to customers (net)	767,513,689
Deferred tax	10,875,800
Other assets	14,157,795
Property and equipment	18,113,251
	2,584,611,248
Liabilities	
Deposits and balances due to Banking institutions	10,396,201
Customer deposits	2,111,202,613
Other liabilities	68,644,434
	2,190,243,248
Net identifiable assets and liabilities (a)	**394,368,000**
Consideration paid (b)	
- satisfied in shares (par value)	250,000,000
- satisfied in shares (share premium)	158,325,000
- satisfied in cash	1,675,000
	410,000,000
Goodwill (b – a)	**15,632,000**
Cash and cash equivalents acquired	
Cash and Bank balances with Central Bank of Kenya (excluding CRR)	85,429,526
Deposits and balances due from Banking institutions	192,623,935
Investments in Government Securities – short term	650,036,802
Less deposits and balances due to Banking institutions	(10,396,201)
Less consideration paid in cash	(1,675,000)
	916,019,062

Notes to the financial statements
for the year ended 31 December 2003 (continued)

	2003 KShs	2002 KShs
4 INTEREST INCOME		
Loans and advances to customers	560,777,656	479,042,099
Government Securities	328,160,799	148,262,376
Placements with other Banks and institutions	32,172,639	25,817,079
	921,111,094	**653,121,554**
5 INTEREST EXPENSE		
Deposit from other Banks and Banking institutions	9,670,131	39,085,112
Customer deposits	286,168,864	291,731,006
	295,838,995	**330,816,118**
6 NON INTEREST INCOME		
Fee and commission income	85,026,068	44,989,116
Rental income	15,449,061	14,265,458
Income from foreign exchange dealings	40,925,285	16,585,261
Other operating income	42,108,370	28,153,361
	183,508,784	**103,993,196**
7 NON INTEREST EXPENSES		
Salaries and employee benefits	165,666,983	91,618,464
Occupancy expenses	37,854,118	13,713,715
Deposit Protection Fund	11,520,763	7,919,182
Depreciation expense	44,929,927	36,566,536
Amortisation expense	1,308,703	1,308,725
Other expenses	142,150,406	91,982,497
	403,430,900	**243,109,119**

The average number of employees engaged during the year were:

	2003	2002
Management	97	57
Unionisable	51	27
Total	**148**	**84**

Included in other expenses are contributions to the defined contribution plan for employees. During the year, the Bank expensed KShs 4,839,141 in contributions payable (2002 – KShs 2,950,905).

Notes to the financial statements
for the year ended 31 December 2003 (continued)

8 PROFIT BEFORE TAXATION

	2003 KShs	2002 KShs
Net income before taxation is arrived at after charging/(crediting):		
Depreciation expense	44,929,927	36,566,536
Amortisation expense	1,308,703	1,308,725
Directors emoluments - As directors	1,500,000	1,500,000
- As executives	4,164,780	3,916,200
Auditors remuneration	1,960,000	1,244,250
(Profit)/loss on sale of property and equipment	(69,660)	114,559

9 TAXATION

	2003 KShs	2002 KShs
Current tax at 30%	96,828,595	41,620,730
Deferred tax (Note 20)	(7,073,247)	7,379,232
	89,755,348	**48,999,962**

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

	2003 KShs	2002 KShs
Accounting profit before tax	**284,833,442**	**108,765,920**
Computed tax using the applicable corporation tax rate @ 30%	85,450,033	32,629,776
Net effect of non-deductible costs and non taxable income	4,305,315	16,370,186
Taxation	**89,755,348**	**48,999,962**

10 EARNINGS PER SHARE

	2003	2002
Net profit for the year	**195,078,094**	**59,765,958**
Weighted average number of ordinary shares in issue during the year (restated)	**10,000,000**	**7,500,000**
Basic earnings per share	**KShs 19.50**	**KShs 7.97**
Diluted earnings per share	**KShs 19.50**	**KShs 5.98**

There were no potentially dilutive shares outstanding at 31 December 2003.

Notes to the financial statements

for the year ended 31 December 2003 (continued)

11 DIVIDEND PER SHARE

	2003 KShs	2002 KShs
The calculation of dividend per share is based on:		
Interim and final dividend declared during the year	100,000,000	45,000,000
Number of ordinary shares as restated	10,000,000	7,500,000
Dividend per share as restated	**10.00**	**6.00**

12 CASH AND BALANCES WITH CENTRAL BANK OF KENYA

	2003 KShs	2002 KShs
Cash in hand	77,229,350	26,170,156
Balances with Central Bank of Kenya:		
– Cash ratio reserve	587,901,240	411,604,535
– Other	115,512,424	121,760,705
	780,643,014	**559,535,396**

The balance with Central Bank of Kenya includes the cash reserve ratio which is non-interest bearing and is based on the value of deposits as adjusted for Central Bank of Kenya requirements. At 31 December 2003 the cash reserve requirement was 6% of eligible deposits (2002 – 10%). These funds are not available to finance the Bank's day-to-day operations.

13 INVESTMENTS IN GOVERNMENT SECURITIES

	2003 KShs	2002 KShs
Treasury Bills		
Maturing within 90 days	277,934,259	312,180,292
Due after 90 days but within one year	317,578,572	125,774,775
Treasury Bonds		
Due within 90 days	652,783,095	189,178,340
Due after 90 days but within one year	665,928,165	195,515,941
Due between 1 and 5 years	2,272,688,737	521,621,968
Total	**4,186,912,828**	**1,344,271,316**

The weighted average effective interest rate on Government securities at 31 December 2003 was 7.12% (2002 – 11.7%).

Notes to the financial statements

for the year ended 31 December 2003 (continued)

14 PLACEMENTS WITH OTHER BANKS

	2003 KShs	2002 KShs
Due within 90 days from date of acquisition	**450,364,993**	**595,397,081**

The weighted average effective interest rate on placements with other Banks at 31 December 2003 was 3.17% (2002 – 9.54%).

15 LOANS AND ADVANCES TO CUSTOMERS

		2003 KShs	2002 KShs
a)	Overdrafts	4,034,767,011	3,167,408,119
	Loans	1,128,815,612	324,269,399
	Bills discounted	181,789,364	30,155,198
	Hire purchase loans	260,723,056	87,948,219
		5,606,095,043	3,609,780,935
	Less: Impairment losses on loans and advances	(290,664,469)	(259,006,365)
		5,315,430,574	**3,350,774,570**

b) Impairment losses on loans and advances

	Specific Impairment losses KShs	General impairment KShs	2003 Total KShs	2002 Total KShs
At 1 January	226,361,329	32,645,036	259,006,365	245,189,321
Effect of acquisition	46,829,368	7,953,712	54,783,080	-
	273,190,697	40,598,748	313,789,445	245,189,321
Impairment made in the year	149,317,412	11,449,045	160,766,457	84,446,150
Recoveries and impairment no longer required	(22,245,535)	-	(22,245,535)	(3,375,822)
Net increase in impairment against revenue	127,071,877	11,449,045	138,520,922	81,070,328
Amounts written off during the year	(161,645,898)	-	(161,645,898)	(67,253,284)
At 31 December 2003	**238,616,676**	**52,047,793**	**290,664,469**	**259,006,365**

Notes to the financial statements

for the year ended 31 December 2003 (continued)

15 LOANS AND ADVANCES TO CUSTOMERS (Continued)

	Specific Impairment losses KShs	General impairment KShs	2003 Total KShs	2002 Total KShs
Net effect on impairment on loans and advances				
Net increase in provisions against revenue	127,071,877	11,449,045	138,520,922	81,070,328
Amounts written off during the year	497,201	-	497,201	(6,646,735)
At 31 December 2003	**127,569,078**	**11,449,045**	**139,018,123**	**74,423,593**

c) Recoveries of loans and advances

	2003 KShs	2002 KShs
Recoveries of loans and advances written off in prior years	**(18,501,582)**	**(6,646,735)**

d) Non performing loans and advances

Loans and advances include an amount of KShs 316,949,562 (2002 - KShs 447,554,481) net of impairment losses. The estimated realisable value of securities held against this balance is KShs 356,653,706 (2002 – KShs 602,624,000).

e) Loans and advances concentration by sector

	2003 KShs	%	2002 KShs	%
Agriculture	353,279,856	6.3	313,942,476	8.7
Manufacturing	1,453,862,868	25.9	945,248,542	26.2
Wholesale and retail trade	713,748,139	12.7	626,227,862	17.3
Building and construction	701,776,748	12.5	446,653,263	12.4
Real estate	227,457,000	4.1	133,872,000	3.7
Electricity and water	63,056,000	1.1	58,560,000	1.6
Finance and insurance	168,085,000	3.0	14,945,000	0.4
Transport and communication	103,620,000	1.8	21,640,000	0.6
Business services	66,266,000	1.2	42,799,000	1.2
Foreign trade	67,418,000	1.2	64,607,000	1.8
Consumer durables	90,777,000	1.6	99,128,000	2.7
Social community services	12,407,000	0.2	3,264,000	0.1
Mining and quarrying	17,759,000	0.3	17,895,000	0.5
Others	1,566,582,432	27.9	820,998,792	22.8
	5,606,095,043	**100.0**	**3,609,780,935**	**100.0**

The weighted average effective interest rate on loans and advances at 31 December 2003 was 10.08% (2002 – 14.3%).

Notes to the financial statements

for the year ended 31 December 2003 (continued)

16 OTHER INVESTMENTS

	2003 KShs	2002 KShs
Short term notes and commercial paper		
Due within 1 year from date of acquisition	31,708,154	32,015,556
Long term notes and commercial papers		
Due between 1 to 5 years from date of acquisition	85,359,679	72,085,653
	117,067,833	**104,101,209**

The weighted average effective interest rate on other investments at 31 December 2003 was 6.39% (2002 – 8.03%).

17 OTHER ASSETS

	2003 KShs	2002 KShs
Rent receivable	4,548	64,080
Prepayments	15,377,974	12,908,799
Other receivables	136,810,582	121,686,690
	152,193,104	**134,659,569**

18 EQUITY INVESTMENT

During the year, the company sold its share holding in I&M Nominees Limited at its carrying value.

	2003 KShs	2002 KShs
At 1 January	499,995	-
(Sold)/Acquired during the year 99,999 shares of KShs 5 each)	(499,995)	499,995
At 31 December	**-**	**499,995**

19 GOODWILL

	2003 KShs	2002 KShs
Goodwill on assets purchased from Biashara Bank of Kenya Limited (Note 3)	15,632,000	-
Amortised during the year	(3,908,001)	-
At 31 December	**11,723,999**	**-**

Management considers this intangible asset to have a useful life of four years and is hence being amortised accordingly.

Notes to the financial statements
for the year ended 31 December 2003 (continued)

20 DEFERRED TAX

Deferred tax liabilities and deferred tax assets at 31 December 2003 and 31 December 2002 are attributable to the following:

	Balance at 01/01/2003 KShs	Effect of acquisition Kshs	Recognised in income KShs	Balance at 31/12/2003 KShs
Plant and equipment	(1,449,624)	8,489,687	5,698,835	12,738,898
Investment property	(4,600,005)	-	(2,060,301)	(6,660,306)
General provisions	9,793,511	2,386,113	3,434,713	15,614,337
Deferred tax @ 30%	**3,743,882**	**10,875,800**	**7,073,247**	**21,692,929**

21 PROPERTY AND EQUIPMENT

	Leasehold improvements Kshs	Furniture, fittings, fixtures & office, equipment KShs	Computers KShs	Motor vehicles KShs	Total KShs
Cost					
At 1 January 2003	119,466,262	78,749,927	94,308,879	13,643,793	306,168,861
Effect on acquisition	72,250,424	39,230,628	24,007,381	7,122,944	142,611,377
Additions	162,250	11,282,125	14,015,451	1,682,830	27,142,656
Disposals	-	(313,164)	(14,964)	(1,193,010)	(1,521,138)
At 31 December 2003	191,878,936	128,949,516	132,316,747	21,256,557	474,401,756
Depreciation					
At 1 January 2003	45,929,231	48,360,222	77,465,992	10,524,520	182,279,965
Effect on acquisition	69,190,788	27,692,754	22,214,764	5,399,818	124,498,124
Charge for the year	13,640,343	13,402,560	15,454,036	2,432,988	44,929,927
Disposals	-	(194,282)	(14,964)	(1,193,010)	(1,402,256)
At 31 December 2003	128,760,362	89,261,254	115,119,828	17,164,316	350,305,760
Net book value					
At 31 December 2003	**63,118,574**	**39,688,262**	**17,196,919**	**4,092,241**	**124,095,996**
At 31 December 2002	**73,537,031**	**30,389,705**	**16,842,886**	**3,119,273**	**123,888,895**

In the opinion of the directors, there is no impairment of property and equipment.

Notes to the financial statements

for the year ended 31 December 2003 (continued)

22 INVESTMENT PROPERTY

	2003 KShs	2002 KShs
Balance as at 1 January	843,608,012	837,338,898
Additions	11,668,933	8,471,472
Disposals	-	(2,202,358)
Balance as at 31 December	**855,276,945**	**843,608,012**

The fair value of the investment property has not been based on a valuation by an independent valuer. The fair value attached to the building is based on a directors' valuation which reflects the best estimate of the replacement cost of putting up the building under the existing market conditions. At the year end the fair value approximates to the original cost of the property and has been stated as such.

The Bank's current lease agreements, which were entered into on an arms-length basis and which are comparable to those of similar properties in the same location, were also taken into account.

The investment property relates to I&M Tower, a commercial property in the Nairobi Central Business District that is leased mainly to third parties. Each of the leases contains an initial non-cancellable period of six years. Subsequent renewals are negotiated with the lessee. No contingent rents are charged. Refer to Note 34(b) for further details.

23 PREPAID OPERATING LEASE RENTALS

Leasehold land	2003 KShs	2002 KShs
At 1 January	115,931,208	117,239,933
Amortisation for the year	(1,308,703)	(1,308,725)
At 31 December	**114,622,505**	**115,931,208**

24 DEPOSITS FROM OTHER BANKS AND BANKING INSTITUTIONS

Payable within 1 year	**114,266,270**	**607,377,812**

The weighted average effective interest rate on deposits from other Banks and Banking institutions at 31 December 2003 was 3.1% (2002 – 7.8%)

25 CUSTOMER DEPOSITS

From Government and Parastatals	2003 KShs	2002 KShs
Payable within 90 days from date of acquisition	-	20,000,000
Payable after 90 days but within one year	15,000,000	52,340,623
	15,000,000	72,340,623

25 CUSTOMER DEPOSITS (continued)

From private sector & individuals	2003 KShs	2002 KShs
Payable within 90 days from date of acquisition	9,778,196,423	5,167,422,159
Payable after 90 days but within one year	346,220,000	122,643,046
Payable between one and five years	2,814,000	1,665,000
	10,142,230,423	**5,364,070,828**

The weighted average effective interest rate on customer deposits at 31 December 2003 was 2.75% (2002 – 6.27%)

26 OTHER LIABILITIES

	2003 KShs	2002 KShs
Bankers cheques payable	100,562,931	22,968,362
Accruals	19,494,637	23,024,103
Other accounts payables	25,159,698	11,239,080
	145,217,266	**57,231,545**

27 SHARE CAPITAL

Authorised, issued and fully paid	2003 KShs	2002 KShs
At 1 January	750,000,000	750,000,000
Issue of new shares		
(2,500,000 ordinary shares of KShs 100 each)	250,000,000	-
At 31 December	**1,000,000,000**	**750,000,000**

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

28 SHARE PREMIUM

2,500,000 ordinary shares of KShs 100 each were issued at a premium of KShs 63.33 per share

	2003 KShs	2002 KShs
At 31 December	**158,325,000**	**-**

Notes to the financial statements

for the year ended 31 December 2003 (continued)

29 NOTES TO THE CASH FLOW STATEMENT

a) Reconciliation of profit before taxation to cashflows from operating activities

	2003 KShs	2002 KShs
Profit before taxation	284,833,442	108,765,920
Depreciation	44,929,927	36,566,536
Amortisation of prepaid operating lease rentals	1,308,703	1,308,725
Amortisation of goodwill	3,908,001	-
(Profit)/Loss on sale of fixed assets	(69,660)	114,559
	334,910,413	**146,755,740**
Increase in operating assets		
Loans and advances to customers	(1,197,142,315)	225,367,281
Other investments	(5,797,707)	(103,704,422)
Investment in government securities	(1,771,396,081)	(542,982,831)
Cash and balances with Central Bank of Kenya		
- Cash Reserve Ratio (CRR)	20,508,119	(29,822,742)
Other assets	(3,375,743)	(68,017,885)
	(2,957,203,727)	**(519,160,599)**
Increase in operating liabilities		
Customer deposits	2,666,956,982	160,656,381
Other liabilities	19,341,287	(26,152,987)
	2,686,298,269	**134,503,394**
Cash generated from operating activities	**64,004,955**	**(237,901,465)**
Taxation paid	(74,651,876)	(6,051,800)
Net cashflows from operating activities	**(10,646,921)**	**(243,953,265)**

b) Analyses of cash and cash equivalents

	2003 KShs	2002 KShs	Change during the year KShs
Cash and balances with Central Bank of Kenya – excluding CRR (Note 12)	192,741,774	147,930,861	44,810,913
Deposits and balances due to Banking institutions	(114,266,270)	(607,377,812)	493,111,542
Deposits and balances due from Banking institutions	450,364,993	595,397,081	(145,032,088)
Investments in government securities (Note 13) – short term	930,717,354	501,358,632	429,358,722
Increase in cash and cash equivalents	**1,459,557,851**	**637,308,762**	**822,249,089**

30 OFF BALANCE SHEET CONTINGENCIES AND COMMITMENTS

In the ordinary course of business, the Bank conducts business involving guarantees, acceptances, letters of credit and bills for collection. These facilities are offset by corresponding obligations of third parties. At the year end, the contingencies were as follows:

	2003 KShs	2002 KShs
Contingencies related to:		
Letters of credit	462,197,379	272,566,999
Guarantees	1,099,035,655	383,212,306
Acceptances	651,995,447	260,310,836
Bills for collection	476,642,651	245,888,153
	2,689,871,132	**1,161,978,294**
Commitments related to :		
Outstanding spot/forward contracts	**402,904,932**	**621,958,988**

Nature of contingent liabilities

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

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

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

Bills for collection is an undertaking by the Bank to collect money from their customers for payment to a third party. They do not bestow any obligations to the Bank.

Forward contracts are arrangements to buy or sell a specified quantity of foreign currency, usually on a specified future date at an agreed rate.

The Bank is a defendant in a number of litigations and claims for which the directors believe, based on the information currently available, that the claims can be successfully defended and therefore no provision has been made in the financial statements.

31 TRUST ACTIVITIES

The Bank provides trust activities to individuals, trusts, retirement benefit plans and other institutions, whereby it holds and manages assets, or invests funds received in various financial instruments at the direction of the customer. The Bank receives fee income for providing these services. Trust assets are not the assets of the Bank and have not been recognised in the balance sheet. The Bank is not exposed to any credit risk relating to such placements as it does not guarantee these investments.

At 31 December 2003, the total assets held by the Bank on behalf of customers was Kshs 243,150,000 (2002 – Kshs 207,467,367).

Notes to the financial statements

for the year ended 31 December 2003 (continued)

31 TRUST ACTIVITIES (continued)

During the year KShs 706,869 was recognized as fee income in the profit and loss account in respect of trust activities (2002 – Kshs 243,967).

32 ASSETS PLEDGED AS SECURITY

As at 31 December 2002 there were no assets pledged by the Bank to secure liabilities and there were no secured Bank liabilities.

33 RELATED PARTY TRANSACTIONS

a) Transactions with directors/shareholders

	2003 KShs	2002 KShs
Loans to related parties	**18,658,000**	**12,171,000**

The related interest income for loans was Kshs 1,537,195 (2002 – Kshs 1,462,606).

b) Transactions with related companies

	2003 KShs	2002 KShs
Guarantees to associate companies	**2,650,000**	**2,050,000**
The fee income earned was Kshs Nil (2002 – Kshs Nil).		
Deposits from related companies	**146,899,907**	**90,084,034**
Interest expense on deposits from related companies was Kshs 5,926,606 (2002 – Kshs 10,904,094).		

c) Transactions with related Banks

	2003 KShs	2002 KShs
Deposits from related Banks	**-**	**179,606,087**
Interest expense on the placements during the year was nil (2002 – Kshs 14,271,610).		

d) Transactions with employees

	2003 KShs	2002 KShs
Staff loans	**26,832,377**	**13,712,689**

Interest earned on these loans was KShs 1,984,262 (2002 – KShs 970,413).

Notes to the financial statements
for the year ended 31 December 2003 (continued)

34 OPERATING LEASES

a) Lessee

The Bank leases six Bank premises under operating leases. The leases typically run for an initial period of six years with an option to renew the lease after that date. None of the leases include contingent rentals. During the year KShs 25,741,477 was charged to the profit and loss account in respect of operating leases (2002 - Kshs 9,008,965).

Future minimum lease payments under these operating leases are as follows:-

	2003 Kshs	2002 Kshs
Less than one year	24,518,382	9,775,526
One to five years	73,125,382	41,428,078
Over five years	-	-
	97,643,764	**51,203,604**

b) Lessor

The company leases out its investment property under operating leases (refer to Note 22). Non-cancellable operating lease rentals are receivable as follows:

	2003 Kshs	2002 Kshs
Less than one year	36,663,479	13,775,513
One to five years	159,901,505	64,212,857
Over five years	273,561,401	187,500
	470,126,385	**78,175,870**

During the year Kshs 13,684,785 was recognized as rental income in the profit and loss account in respect of operating leases (2002 – Kshs 14,265,458). In addition, Kshs 8,041,169 in respect of management expenses was recognized as an expense in the profit and loss account in respect of investment property (2002 – Kshs 12,399,932).

35 CAPITAL COMMITMENTS

	2003 Kshs	2002 Kshs
Authorised and contracted for	**3,169,959**	**3,715,200**

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37 INTEREST RATE RISK – Page 38

38 CURRENCY RISK – Page 40

39 FINANCIAL RISK MANAGEMENT DISCLOSURES

This section provides details of the Bank's exposure to risk and describes the methods used by management to control risk. The most important types of financial risk to which the Bank is exposed are liquidity risk as detailed in Note 36, credit risk and market risk. Market risk includes currency risk and interest rate risk.

(A) Derivative financial instruments

The Bank enters into forward foreign exchange contracts for trading purposes with third parties as well as for managing its own liquidity and foreign currency exposures.

Forward foreign exchange contracts are commitments to either purchase or sell a designated financial instrument at a specified date for a specified price and may be settled in cash or another financial asset. Forward contracts result in credit exposure to the counter-party and exposure to market risk based on changes in market prices relative to contracted amounts.

(B) Trading activities

The Bank manages its trading activities by type of risk involved and on the basis of the categories of trading instruments held.

(i) Credit risk

The Bank's credit exposure at the balance sheet date from financial instruments held or issued for trading purposes is represented by the fair value of instruments with a positive fair value at that date, as recorded on the balance sheet.

The risk that the counter-parties to trading instruments might default on their obligation is monitored on an ongoing basis. In monitoring credit risk exposure, consideration is given to trading instruments with a positive fair value and to the volatility of the fair value of trading instruments over their remaining life.

To manage the level of credit risk, the Bank deals with counter parties of good credit standing, enters into master netting agreements wherever possible and when appropriate, obtains collateral.

Master netting agreements provide for the net settlement of contracts with the same counter-party in the event of default

An assessment of the extent to which fair values of collaterals cover existing credit risk exposure on loans and advances to customers is highlighted in Note 16(d) of these financial statements.

The Bank also monitors concentrations of credit risk that arise by industry and type of customer in relation to the Bank loans and advances to customers by carrying a balanced portfolio. The Bank has no significant exposure to any individual customer or counter-party.

(ii) Market risk

All trading instruments are subject to market risk, the risk that the future changes in market conditions may make an instrument less valuable or more onerous. The Bank manages its use of trading instruments in response to changing market conditions. Exposure to market risk is formally managed in accordance with risk limits set by senior management and the asset liability committee.

Notes to the financial statements
for the year ended 31 December 2003 (continued)

(iii) Liquidity risk

Liquidity risk includes the risk of being unable to liquidate assets at a reasonable price and in an appropriate timeframe in order to meet the Banks financial obligation as they fall due.

The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall Bank strategy. In addition, the Bank holds a portfolio of liquid assets as part of its liquidity risk management strategy.

(iv) Currency risk

The Bank operates wholly within Kenya and its assets and liabilities in these financial statements are reported in the local currency. The Bank maintains operating accounts with other correspondent Banks. Foreign currency positions are monitored and managed within limits set by senior management as well as within the local regulatory guidelines.

40 INCORPORATION

The Bank is incorporated as a limited company in Kenya under the Companies Act and is licensed under the Banking Act.

41 CURRENCY

These financial statements are expressed in Kenya Shillings (KShs).

36 LIQUIDITY RISK

Contractual maturity analysis of assets and liabilities

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period at 31 December 2003 to the contractual maturity date.

	31 December 2003						31 December 2002					
	On Demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years	Total	On Demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years	Total
	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Assets												
Goodwill	-	-	-	11,724	-	**11,724**						
Cash and balances with Central Bank of Kenya	780,643	-	-	-	-	**780,643**	147,930	-	-	-	411,605	**559,535**
Investments in government securities	-	930,717	983,507	2,272,689	-	**4,186,913**	-	501,358	321,291	521,622	-	**1,344,271**
Placements with other Banks	217,293	233,072	-	-	-	**450,365**	346,400	248,997	-	-	-	**595,397**
Loans and advances to customers (net)	3,759,946	159,320	164,061	1,051,950	180,153	**5,315,430**	3,210,061	13,831	109,182	17,701	-	**3,350,775**
Other investments	-	26,785	4,923	85,360	-	**117,068**	-	32,016	-	72,085	-	**104,101**
Equity investment	-	-	-	-	-	**-**	500	-	-	-	-	**500**
Taxation	-	-	-	-	-	**-**	-	-	-	-	-	**-**
Deferred tax	-	-	-	-	21,693	**21,693**	-	-	-	-	3,744	**3,744**
Other assets	152,193	-	-	-	-	**152,193**	134,660	-	-	-	-	**134,660**
Property and equipment	-	-	-	-	124,096	**124,096**	-	-	-	-	123,889	**123,889**
Investment property	-	-	-	-	855,277	**855,277**	-	-	-	-	843,608	**843,608**
Prepaid operating lease rentals	-	-	-	-	114,623	**114,623**	-	-	-	-	115,931	**115,931**
Total assets	4,910,075	1,349,894	1,152,491	3,421,723	1,295,842	**12,130,025**	3,839,551	796,202	430,473	611,408	1,498,777	**7,176,411**
Liabilities and equity												
Deposits from other Banks	-	114,267	-	-	-	**114,267**	192,815	414,563	-	-	-	**607,378**
Customer deposits	3,554,549	6,390,895	193,978	2,808	-	**10,142,230**	618,872	4,568,550	174,984	1,665	-	**5,364,071**
Taxation	-	32,230	-	-	-	**32,230**	-	10,053	-	-	-	**10,053**
Other liabilities	145,217	-	-	-	-	**145,217**	57,231	-	-	-	-	**57,231**
Equity	-	-	-	-	1,696,081	**1,696,081**	-	45,000	-	-	1,092,678	**1,137,678**
Total liabilities & equity	**3,699,766**	**6,537,392**	**193,978**	**2,808**	**1,696,081**	**12,130,025**	**868,918**	**5,038,166**	**174,984**	**1,665**	**1,092,678**	**7,176,411**
Net Liquidity Gap	**1,203,333**	**(5,178,356)**	**958,513**	**2,296,302**	**720,208**	**-**	**2,970,633**	**(4,241,964)**	**255,489**	**609,743**	**406,099**	**-**

The customer deposits on 1-3 months relate to fixed deposits account balances. Although classified in this band, previous experience has shown these are normally rolled over and are therefore of a long term nature.

Notes to the financial statements

for the year ended 31 December 2003 (continued)

37 INTEREST RATE RISK ANALYSIS

The following table indicates the effective interest rate at the balance sheet date and the periods in which financial assets and liabilities reprice

	31 December 2003								31 December 2002							
	Effective interest rate	On demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years	Non interest bearing	Total	Effective interest rate	On demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years	Non interest bearing	Total
	%	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	%	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Assets																
Goodwill	-	-	-	-	-	-	11,724	**11,724**								
Cash and balances with Central Bank of Kenya	-	-	-	-	-	-	780,643	**780,643**	-	-	-	-	-	-	559,535	**559,535**
Investments in government securities	7.12%	-	930,717	983,507	2,272,689	-	-	**4,186,913**	11.70%	-	501,358	321,291	521,622	-	-	**1,344,271**
Placements with other Banks	3.17%	217,293	233,072	-	-	-	-	**450,365**	9.54%	346,400	248,997	-	-	-	-	**595,397**
Loans and advances to customers (net)	10.08%	3,588,407	159,320	164,061	1,051,950	180,153	171,539	**5,315,430**	14.30%	2,798,575	13,831	109,182	17,701	-	411,486	**3,350,775**
Other investments	6.39%	-	26,785	4,923	85,360	-	-	**117,068**	8.03%	-	32,016	-	72,085	-	-	**104,101**
Equity investment	-	-	-	-	-	-	-	**-**	-	-	-	-	-	-	500	**500**
Taxation	-	-	-	-	-	-	-	**-**	-	-	-	-	-	-	-	**-**
Deferred tax	-	-	-	-	-	-	21,693	**21,693**	-	-	-	-	-	-	3,744	**3,744**
Other assets	-	-	-	-	-	-	152,193	**152,193**	-	-	-	-	-	-	134,660	**134,660**
Property and equipment	-	-	-	-	-	-	124,096	**124,096**	-	-	-	-	-	-	123,889	**123,889**
Investment property	-	-	-	-	-	-	855,277	**855,277**	-	-	-	-	-	-	843,608	**843,608**
Prepaid operating lease rentals	-	-	-	-	-	-	114,623	**114,623**	-	-	-	-	-	-	115,931	**115,931**
Total assets		**3,805,700**	**1,349,894**	**1,152,491**	**3,409,998**	**180,153**	**2,231,792**	**12,130,025**	**3,144,975**	**796,202**	**430,473**	**611,403**	**-**	**-**	**2,193,353**	**7,176,411**

37 INTEREST RATE RISK ANALYSIS (continued)

	31 December 2003								31 December 2002							
	Effective interest rate	On demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years	Non interest bearing	Total	Effective interest rate	On demand	Due within 3 months	Due between 3 and 12 months	Due between 1 and 5 years	Due after 5 years	Non interest bearing	Total
	%	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	%	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Liabilities and equity																
Deposits from other Banks	3.10%	-	114,267	-	-	-	-	**114,267**	7.80%	192,815	414,563	-	-	-	-	**607,378**
Customer deposits	2.75%	3,554,549	6,390,895	193,978	2,808	-	-	**10,142,230**	6.27%	618,872	4,568,550	174,984	1,665	-	-	**5,364,071**
Taxation	-	-	-	-	-	-	32,230	**32,230**	-	-	-	-	-	-	10,053	**10,053**
Other liabilities	-	-	-	-	-	-	145,217	**145,217**	-	-	-	-	-	-	57,231	**57,231**
Equity	-	-	-	-	-	-	1,696,081	**1,696,081**	-	-	-	-	-	-	1,137,678	**1,137,678**
Total liabilities and equity		**3,554,549**	**6,505,161**	**193,978**	**2,808**	**-**	**1,873,528**	**12,130,025**		**811,687**	**4,983,113**	**174,984**	**1,665**	**-**	**1,204,962**	**7,176,411**
On balance sheet interest rate sensitivity gap		**251,151**	**(5,146,127)**	**958,513**	**2,296,302**	**1,098,463**	**541,697**	**-**		**2,333,288**	**(4,186,911)**	**255,489**	**609,743**	**-**	**988,391**	**-**

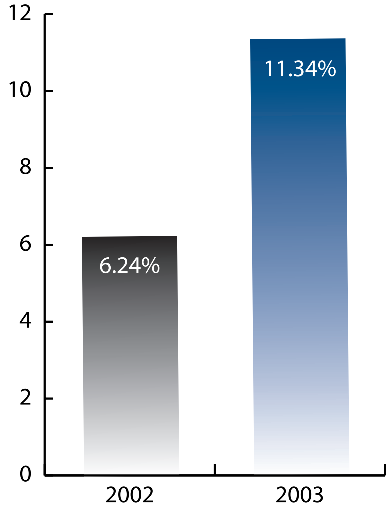
38 FOREIGN CURRENCY RISK ANALYSIS

The table below analyses the currencies to which the Bank is exposed as at 31 December 2003:

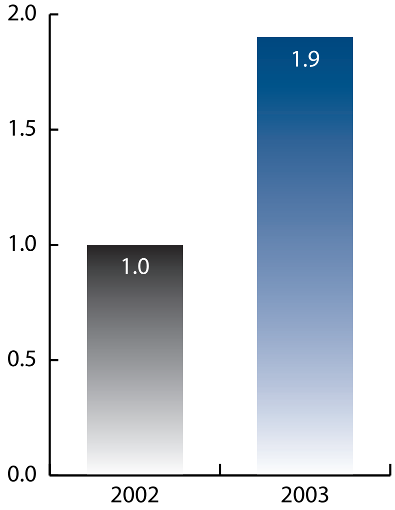
	31 December 2003					31 December 2002				
	USD	GBP	EURO	Others	Total	USD	GBP	EURO	Others	Total
	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Assets										
Balance Sheet Items										
Cash and balances with Banks abroad	(6,622)	177,414	44,623	78,189	**293,604**	208,680	165,106	52,378	123,806	**549,970**
Loans and advances	908,300	92,452	43,910	40	**1,044,702**	704,153	20,613	-	-	**724,766**
Other foreign assets	-	85,360	-	-	**85,360**	-	72,055	-	-	**72,055**
Off Balance Sheet Items										
Undelivered spot purchases	111,684	19,648	23,905	-	**155,237**	263,854	-	-	-	**263,854**
Forward purchases	45,930	182,932	-	-	**228,862**	-	123,142	-	-	**123,142**
Total foreign assets	**1,059,292**	**557,806**	**112,438**	**78,229**	**1,807,765**	**1,176,687**	**380,916**	**52,378**	**123,806**	**1,733,787**
Liabilities										
Balance Sheet Items										
Customer deposits	791,457	493,230	36,050	74,520	**1,395,257**	680,051	363,121	77,384	121,863	**1,242,419**
Deposits due to Banking institutions	19,041	36,079	19,137	-	**74,257**	41,768	81,252	-	-	**123,020**
Off Balance Sheet Items										
Undelivered spot sales	62,524	25,068	5,355	-	**92,947**	234,964	-	4,869	-	**239,833**
Forward sales	178,966	-	47,810	-	**226,776**	123,142	-	-	-	**123,142**
Total foreign liabilities	**1,051,988**	**554,377**	**108,352**	**74,520**	**1,789,237**	**1,079,925**	**444,373**	**82,253**	**121,863**	**1,728,414**
Net open position	**7,304**	**3,429**	**4,086**	**3,709**	**18,528**	**96,762**	**(63,457)**	**(29,875)**	**1,943**	**5,373**

I&M - Biashara Bank merger synergy

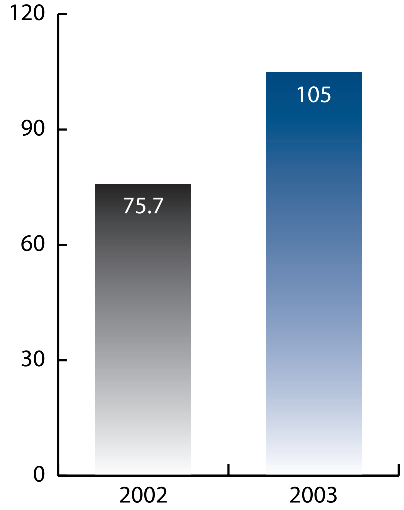
Return on Capital Employed (Ksh. million)



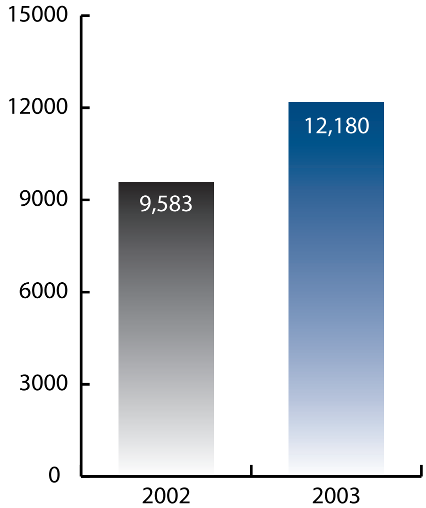
Profit Before Tax/Employee (Ksh. million)



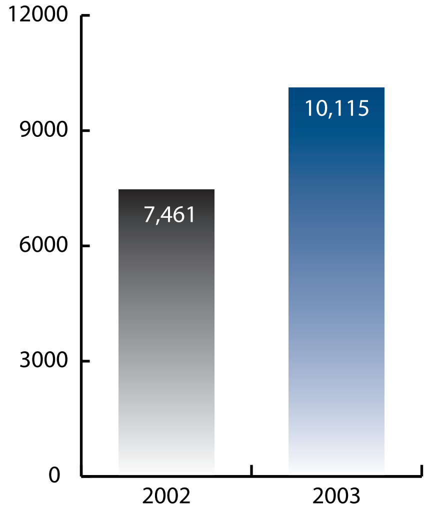
Business Volumes/Employee (Ksh. million)



Total Assets (Ksh. million)



Customer Deposits (Ksh. million)



I&M & Biashara

I&M

I&M Bank Corporate Social Responsibility

Like in previous years, I&M Bank had a full year's calendar of charitable activities in 2003. Staff at all levels get involved in these activities which represent the Bank's commitment to contribute to the society in which it thrives:

Date	To	Items donated
January, 2003	Nyumbani –Children of God Relief Institute	Bathing towels and ink cartridges
February, 2003	Renu Sasodia & Children	School fees, uniforms, shoes, school books, foodstuff
February, 2003	Starehe Boys' Centre	To a needy child
April, 2003	SSL, MP Shah Hospital	Towards construction
April, 2003	My dream – Young Jains	Towards education
May, 2003	Oshwal Youth League	Platinum Games
May, 2003	Visa Oshwal Nursery School	Donation
May, 2003	Karuna Charity Trust	Advertising in a commemorative magazine/souvenir
May, 2003	Sarit's Centre's 20th Anniversary Charity Raffle in aid of Nyumbani & Hope Homes for HIV+ children	Cash
July, 2003	Kibagare Good News Centre	Foodstuff
July, 2003	Nyumbani	Foodstuff, kitchen requirements, books and pens
August, 2003	Lions Club Nairobi Central	Golf sponsorship to carry out major eye operations in Kenya
September, 2003	SSL, MP Shah Hospital	Towards construction
November, 2003	Ebenezer Children's Home	Foodstuff
November, 2003	Ebenezer Children's Home	Foodstuff
December, 2003	Nyumbani	Foodstuff

Mr Sarit Shah, Executive Director of I&M Bank and other staff members hand over foodstuff to the Kibagare Good News Centre

Advertising Campaign - New Products

To promote the newly launched ATMS through the Kenswitch network, the Bank undertook a major retail campaign called 'I&M ATM ACCOUNT CAMPAIGN'. All holders of I&M Bank ATM cards during the campaign period were eligible to win One Million Shillings in a Grand Draw. The campaign succeeded in significantly increasing the number of retail customers of the Bank and also more than doubled the number of existing account holders who applied for the I&M Bank ATM card.

Advertising Campaign - New Products

The Bank has introduced a popular new product called 'I&M Home Loans' signifying a formal entry into the Home Mortgages market. The product was launched with a series of innovative advertisements, which generated a huge response.