Stanbic Bank Kenya Limited

Annual Report and Financial Statements

For the year ended 31 December 2018

Table of contents

Corporate information

Corporate Information

Financial statements

Financial Statements

Corporate information

Chairman:	Fred N. Ojiambo, MBS, SC
Chief Executive:	Charles Mudiwa***
Chief Executive of Stanbic Holdings Plc:	Greg Brackenridge*
Non-Executive Directors:	Kitili Mbathi Rose Kimotho Edward W. Njoroge Ruth T. Ngobi Peter N. Gethi Christopher J. Blandford – Newson** Rose B. Osoro Dorcas Kombo
	* South African ** South African and British *** Zimbabwean
Company Secretary:	Lillian N. Mbindyo P.O. Box 72833 00200 Nairobi
Auditor:	PricewaterhouseCoopers PwC Tower Waiyaki Way/Chiromo Road P.O. Box 43963 00100 Nairobi
Registered Office:	Stanbic Bank Centre Chiromo Road, Westlands P.O. Box 72833 00200 Nairobi

Report of the Directors

The Directors submit their report together with the audited financial statements for the year ended 31 December 2018, which disclose the state of affairs of Stanbic Bank Kenya Ltd (the “Bank” or the “Company”).

Principal activities

The Bank is a licensed financial institution under the Banking Act (Cap 488) and is a member of the Kenya Bankers Association.

The Bank is engaged in the business of banking and the provision of related banking services.

Business review

The Bank has exposure to various risks from its operations. These are -:

a) Credit risk
b) Liquidity risk
c) Market risk
d) Operational risk

These are explained in more detail on Note 4 of the financial statements.

Business review and financial performance

The Bank reported an improvement in earnings because of improved client revenues, increased trading revenues and a lower impairment charge during the year. The Bank mobilised technology to enhance client experience and improve operational efficiency. The balance sheet continued to show strong growth as the Bank focussed on creating value and delightful experiences for its customers.

During the year, the Bank refined its strategy to remain relevant in its role as a financial services provider while delivering superior stakeholder value.

Some of the major highlights were-:

a) The profit after tax was KShs 6.2b (2017: KShs 4.3b);

b) Net interest income grew to KShs 12.1b compared to KShs 10.6b over the same period in 2017 due to a 12% growth in customer loans and advances. In addition, the growth in transactional accounts resulted in lower cost of funds;

c) Non interest revenue reported a strong performance as the Bank leveraged on technology to improve its customers’ banking experience and successful closure of key deals in Investment Banking;

d) Loan loss provisions decreased during the year as the Bank continues to focus on proactive arrears management; and

e) The Bank continued to focus on customer acquisition as evidenced in the growth of customer deposits which grew by 24% during the year.The growth was largely on current accounts and savings accounts which grew by 13% and 62% respectively.

South Sudan economy continued to suffer from the ongoing political instability and the effects of a hyper inflationary environment. Despite this, the Bank's South Sudan branch remained profitable with strong growth on customer deposits. The Bank continues to be proactive in risk management and remain prudent on costs. The Branch's on the ground activities continue to be transactional and liability led.

The Bank expects to sustain its performance in the year 2019 by focusing on growing our target clients in Corporate and Investment Banking and scaling up Personal and Business banking. It will continue to proactively monitor some of its customers currently in distress and assess the level of impairment charges held for these exposures.

Dividends

In the current year, the Directors paid an interim dividend of KShs 5.28 (2017: KShs 2.93) per ordinary share equivalent to a total sum of KShs 900 million (2017: KShs 500 million).

Subject to the approval of the shareholders at the 2019 Annual General Meeting, the Directors recommend payment of a final dividend of KShs 7.62 (2017: KShs 9.38) per ordinary share equivalent to a total sum of KShs 1,300 million (2017: KShs 1,600 million). The total dividend for the year, therefore, will be KShs 12.90 (2017: KShs 12.31) for every one ordinary share amounting to KShs 2,200 million (2017: KShs 2,100 million).

The total number of issued shares at year end was 170,577,426 (2017: 170,577,426).

The results for the year are set out fully on pages 12 to 134 in the attached financial statements.

Directors

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

Events subsequent to the end of the reporting period

There is no material event that has occurred between the end of the reporting period and the date of this report.

Management by third parties

There is no aspect of the business of the Bank that has been managed by a third person or a company in which a director has had an interest during the year.

Auditor

Disclosures to auditor

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

a) there was, as far as each director is aware, no relevant audit information of which the company's auditor is unaware; and

b) each director had taken all steps that ought to have been taken as a director so as to be aware of any relevant audit information and to establish that the company's auditor is aware of that information.

Terms of Appointment of Auditor

PricewaterhouseCoopers continue in office in accordance with the Company's Articles of Association and Section 719 of the Kenyan Companies Act, 2015.

The directors monitor the effectiveness, objectivity and independence of the auditor. This responsibility includes the approval of the audit engagement contract and the associated fees on behalf of the shareholders.

Approval of financial statements

The financial statements were approved by the Board of Directors on 28 February 2019.

By Order of the Board,

L.N. Mbindyo
Company Secretary
28 February 2019

Statement of Directors' responsibilities

The Kenyan Companies Act, 2015 requires the directors to prepare financial statements for each financial year that give a true and fair view of the financial position of the Company as at the end of the financial year and of their profit or loss for that year. It also requires the directors to ensure that the Company keeps proper accounting records that: (a) show and explain the transactions of the Company; (b) disclose, with reasonable accuracy, the financial position of the Company; and (c) enable the directors to ensure that every financial statement required to be prepared complies with the requirements of the Kenyan Companies Act, 2015.

The directors accept responsibility for the preparation and presentation of these financial statements in accordance with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. They also accept responsibility for:

i) designing, implementing and maintaining such internal control as they determine necessary to enable the presentation of financial statements that are free from material misstatement, whether due to fraud or error;

ii) selecting suitable accounting policies and applying them consistently; and

iii) making accounting estimates and judgements that are reasonable in the circumstances.

Having made an assessment of the Company's ability to continue as a going concern, the directors are not aware of any material uncertainties related to events or conditions that may cast doubt upon the Company's ability to continue as a going concern.

The directors acknowledge that the independent audit of the financial statements does not relieve them of their responsibilities.

Approved by the Board of Directors on **28 February 2019** and signed on its behalf by:

....
Chairman
FRED N. OJIAMBO, MBS, SC

....
Director

....
Chief Executive
CHARLES MUDIWA

Independent auditor's report to the Shareholders of Stanbic Bank Kenya Limited

Report on the audit of the financial statements

Opinion

We have audited the accompanying financial statements of Stanbic Bank Kenya Limited (the "Bank" or "Company") set out on pages 12 to 134 which comprise the statement of financial position at 31 December 2018 and the statements of profit or loss, other comprehensive income, changes in equity and cash flows for the year then ended and the notes to the financial statements, which include a summary of significant accounting policies.

In our opinion, the financial statements give a true and fair view of the financial position of Stanbic Bank Kenya Limited at 31 December 2018 and of its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of 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 *Auditor's responsibilities for the audit of the financial statements* section of our report.

We are independent of the 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 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 Bank's financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	***How our audit addressed the matter***
Credit risk and provision for expected credit losses on financial assets The Bank implemented IFRS 9 on 1 January 2018. The standard requires the Bank to recognise expected credit losses (ECLs) on financial instruments.	We obtained an understanding of the Bank's IFRS 9 implementation process including the governance processes thereof through discussions with management and review of related documentation.

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Independent auditor's report to the Shareholders of Stanbic Bank Kenya Limited (continued)

Key audit matter	*How our audit addressed the matter*
Credit risk and provision for expected credit losses on financial assets (continued)	
As explained in notes 2.5 and 3.2 of these financial statements, determining ECL is complex, judgmental and involves estimation uncertainty. IFRS 9 requires the Directors to measure ECLs on a forward looking basis reflecting a range of future economic conditions. Changes to the assumptions and estimates used by management could generate significant fluctuations in the Bank's financial performance, and materially impact the valuation of the Bank's portfolio of financial assets. The ECL determination process for both business segments of the Bank as well as the impact of adoption of IFRS is detailed in Notes 3.11 and 2 (c) respectively of these financial statements. Auditing the Bank's ECL as computed was deemed an area of most significance to our audit due to the inherent subjectivity of the assumptions and judgment made by management in: (a) estimation of default events that may happen during the lifetime of the instruments, and the probability weighting thereof; (b) application of qualitative information in determining staging of exposures; and (c) application of complex modelling assumptions used to build the models that calculate ECL, completeness and accuracy of data used to calculate the ECL and the accuracy and adequacy of the financial statement disclosures.	We reviewed and assessed management's accounting policies over key IFRS 9 concepts especially significant increase in credit risk (SICR), default definition, forecasting of forward looking macro-economic factors, and weighting of expected loss scenarios. For a sample of contracts, we tested the identification of financial assets that have experienced SICR or met the Bank's default definition criteria for purposes of staging. This was done through examining documentation and credit performance to form an independent judgment as to whether the staging of such facilities was in line with the Bank's policy. For stage 3 facilities, we selected a sample of financial assets and examined the reasonableness of the expected future recoverable amounts as assessed by management to support the calculation of the ECL thereon. We assessed the assumptions and compared estimates to both internal and external evidence, where available. Where impairment was calculated using a model (stages 1 & 2), we tested the basis and operation of those models and the data and assumptions used. Our audit procedures included: - Comparison of the principal assumptions made with our own knowledge of other practices and actual experience. - Testing the operation of the models used to calculate the impairment including, in some cases, developing independent expectations and comparing results. - Assessed overlays made by management over and above the formulaic computed ECLs. - Reviewed management's ECL related disclosures especially on areas with the highest estimation levels.

Independent auditor's report to the Shareholders of Stanbic Bank Kenya Limited (continued)

Key audit matter	*How our audit addressed the matter*
Potential exposure arising from a material guarantee contract	
As disclosed in Note 42.1 of the financial statements, the Bank is party to a material guarantee contract whereby the contracting parties have had performance disagreements. This exposes the bank to a potential payout, subject to progression and /or finalisation of ongoing dispute resolution mechanisms. The amounts involved can be potentially significant, and the application of IAS 37: Provisions, Contingent Liabilities and Contingent Assets to estimate the expected outflow, if any, of any liability to be recognised is inherently subjective. The directors exercised significant judgements and assumptions in determining the likelihood of a liability crystallising from the guaranteed contract, and the estimation of any provisions at year end. The outcome of the ongoing dispute resolution mechanisms could be materially different from management's estimation.	We enquired of the directors and management of the progress of the matter and their assessment as to its potential to crystallise to a liability for the Bank. We also reviewed documentation available including contract terms, minutes of meetings and legal opinions, to evaluate the basis and reasonableness of provisions made. We reviewed the disclosures made in the financial statements regarding the matter to assess whether they detail the potential liabilities and the significant uncertainties that exist.

Other information

The other information comprises Corporate Information, Report of the Directors and Statement of Directors' Responsibilities which we obtained prior to the date of this auditor's report, and the rest of the other information in the Annual Report which are expected to be made available to us after that date, but does not include the financial statements and our auditor's report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and we do not and will 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 identified above 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 on the other information we have received prior to the date of this auditor's report 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.

When we read the rest of the other information in the Annual Report and we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

Independent auditor's report to the Shareholders of Stanbic Bank Kenya Limited (continued)

Responsibilities of the directors for the financial statements

The directors are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards and the requirements of 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, the directors are responsible for assessing the 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 Company or to cease operations, or have no realistic alternative but to do so.

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

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism 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.

- 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 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 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 auditor's 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 auditor's report. However, future events or conditions may cause 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.

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

Independent auditor's report to the Shareholders of Stanbic Bank Kenya Limited (continued)

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on 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 auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other matters prescribed by the Kenyan Companies Act, 2015

Report of the Directors

In our opinion the information given in the Report of the Directors on pages 4 and 5 is consistent with the financial statements.

PricewaterhouseCoopers

Certified Public Accountants
Nairobi

1 MARCH 2019

CPA Kang'e Saiti, Practising certificate No. 1652
Signing partner responsible for the independent audit

Statement of profit or loss

	Note	Year ended 31 December 2018 KShs'000	2017 KShs'000
Interest income	7	19,209,386	16,592,500
Interest expense	7	(7,157,013)	(6,004,664)
Net interest income		**12,052,373**	**10,587,836**
Credit impairment losses	26.3	(2,064,462)	(2,761,325)
Net income after credit impairment losses		**9,987,911**	**7,826,511**
Fees and commission income	8	4,445,085	3,947,733
Fees and commission expense	9	(430,944)	(401,215)
Net fees and commission income		**4,014,141**	**3,546,518**
Trading revenue	10	5,350,669	3,826,785
Net income from financial instruments at fair value through profit and loss	11	40,938	576,477
Other income	12	18,408	109,980
Other gains and losses on financial instruments[1]	22.1	891	-
Net trading and other income		**5,410,906**	**4,513,242**
Net operating income		**19,412,958**	**15,886,271**
Employee benefits expense	13	(5,651,978)	(5,569,321)
Depreciation	30	(415,413)	(378,665)
Amortisation of intangible assets	31	(191,804)	(178,580)
Finance costs	15	(93,579)	(283,452)
Other operating expenses		(4,274,966)	(4,063,303)
Total operating expenses		**(10,627,740)**	**(10,473,321)**
Profit before income tax		**8,785,218**	**5,412,950**
Income tax expense	16	(2,609,146)	(1,073,814)
Profit for the year		**6,176,072**	**4,339,136**
Earnings per share			
Basic and diluted (KShs per share)	17	36.21	25.44

1 The Bank, as permitted by IFRS 9, elected not to restate their comparative annual financial statements. Therefore, comparability will not be achieved by the fact that the comparative financial information has been prepared on an IAS 39 basis. Refer to the accounting policy elections, IFRS 9 transition on Note 2 for more detail.

The notes set out on pages 18 to 134 form an integral part of these financial statements.

Statement of other comprehensive income

	Note	Year ended 31 December 2018 KShs'000	2017 KShs'000
Profit for the year		**6,176,072**	**4,339,136**
Total other comprehensive income, net of income tax			
Items that may subsequently be reclassified to profit or loss			
Net change in fair value movements on available-for-sale financial assets-IAS 39[1]	22 (b)	N/A	298,645
Net change in debt financial assets measured at fair value through other comprehensive income (OCI) - IFRS 9[1]	22 (b)	(320,469)	N/A
Net gain on financial assets measured at FVOCI	22 (b)	(891)	N/A
Currency translation differences for foreign operations		(268,351)	73,788
Total other comprehensive income for the year, net of income tax		**(589,711)**	**372,433**
Total comprehensive income for the year		**5,586,361**	**4,711,569**

[1] *The Bank, as permitted by IFRS 9, elected not to restate their comparative annual financial statements. Therefore, comparability will not be achieved by the fact that the comparative financial information has been prepared on an IAS 39 basis. Refer to the accounting policy elections, IFRS 9 transition on Note 2 for more detail.*

The notes set out on pages 18 to 134 form an integral part of these financial statements.

Statement of financial position	**Note**	**As at 31 December 2018 KShs'000**	**2017 KShs'000**
Assets			
Cash and balances with Central Bank of Kenya	20	22,061,875	8,044,783
Financial assets – held for trading	21	31,202,035	29,806,020
Financial investments – (FVOCI/available-for-sale)	22	17,851,517	40,988,774
Financial investments – (amortised cost/held to maturity)	23	23,200,956	5,444,178
Derivative assets	24	1,515,466	2,391,101
Loans and advances to banks	25	28,294,576	12,640,509
Loans and advances to customers	26	146,604,117	130,535,810
Other assets and prepayments	27	3,732,194	3,647,840
Other investments	29	17,500	17,500
Investments in subsidiaries	28	2	2
Property and equipment	30	2,234,257	2,305,419
Other intangible assets	31	1,032,610	1,080,514
Current tax asset	33	-	16,667
Deferred tax asset	32	3,205,907	2,488,760
Total assets		**280,953,012**	**239,407,877**
Equity and liabilities			
Liabilities			
Deposits from customers	34	192,258,013	155,405,963
Deposits from banks	35	27,909,240	38,707,135
Current tax liability	33	1,097,202	-
Deferred tax liability	32	-	38,859
Derivative liabilities	24	1,881,658	2,427,563
Trading liabilities	21	10,373,068	362,630
Other liabilities and accruals	36	5,779,102	5,425,290
Borrowings	37	7,064,013	3,989,243
Total liabilities		**246,362,296**	**206,356,683**
Shareholders' equity			
Ordinary share capital	38	3,411,549	3,411,549
Ordinary share premium	39	3,444,639	3,444,639
Regulatory credit risk reserve	40	938,245	73
Translation reserve	40	(1,064,130)	(795,779)
Revenue reserves		26,381,053	24,908,793
Proposed dividend	18	1,300,000	1,600,000
FVOCI/available-for-sale reserve	40	21,957	343,317
Revaluation reserve	40	122,598	122,598
Share based payment reserve	41	34,805	16,004
Total shareholders' equity		**34,590,716**	**33,051,194**
Total equity and liabilities		**280,953,012**	**239,407,877**

The notes set out on pages 18 to 134 form an integral part of these financial statements.

The financial statements on pages 12 to 134 were approved for issue by the Board of Directors on 28 February 2019 and signed on its behalf by:

Chairman .... FRED N. OJIAMBO, MBS, SC

Chief Executive .... CHARLES MUDIWA

Director .... KITILI MBATHI

Company Secretary .... LILLIAN MBINDYO

Statement of changes in equity

Year ended 31 December 2018	Note	Share capital	Share premium	Regulatory credit risk reserve	Foreign currency translation reserve	Revaluation of financial assets-Fair value through OCI	Revaluation reserve on buildings	Share-based payment reserve	Retained earnings	Proposed dividend	Total equity
		KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
At 1 January 2018		3,411,549	3,444,639	73	(795,779)	343,317	122,598	16,004	24,908,793	1,600,000	**33,051,194**
Impact of initial application of IFRS 9[1]	2	-	-	(73)	-	-	-	-	(1,565,567)	-	**(1,565,640)**
		3,411,549	**3,444,639**	**-**	**(795,779)**	**343,317**	**122,598**	**16,004**	**23,343,226**	**1,600,000**	**31,485,554**
Profit for the year		-	-	-	-	-	-	-	6,176,072	-	**6,176,072**
Other comprehensive income, net of tax		-	-	-	(268,351)	(321,360)	-	-	-	-	**(589,711)**
Total comprehensive income for the year		**-**	**-**	**-**	**(268,351)**	**(321,360)**	**-**	**-**	**6,176,072**	**-**	**5,586,361**
Transfer from regulatory credit risk reserve	40	-	-	938,245	-	-	-	-	(938,245)	-	**-**
Transactions with owners recorded directly in equity											
Equity-settled share-based payment transactions	41	-	-	-	-	-	-	18,801	-	-	**18,801**
2018 Interim and 2017 final dividend paid	18	-	-	-	-	-	-	-	(900,000)	(1,600,000)	**(2,500,000)**
2018 Final dividend proposed	18	-	-	-	-	-	-	-	(1,300,000)	1,300,000	**-**
Total transactions with owners		**-**	**-**	**-**	**-**	**-**	**-**	**18,801**	**(2,200,000)**	**(300,000)**	**(2,481,199)**
At 31 December 2018		**3,411,549**	**3,444,639**	**938,245**	**(1,064,130)**	**21,957**	**122,598**	**34,805**	**26,381,053**	**1,300,000**	**34,590,716**

[1] *Refer to the accounting policy elections, IFRS 9 transition on note 2 for more detail on the IFRS 9 transition.*

The notes set out on pages 18 to 134 form an integral part of these financial statements.

Statement of changes in equity (continued)

Year ended 31 December 2017	Not	Share capital KShs'000	Share premium KShs'000	Regulatory credit risk reserve KShs'000	Foreign currency translation reserve KShs'000	Revaluation of financial assets available-for-sale KShs'000	Revaluation reserve on buildings KShs'000	Share-based payment reserve KShs'000	Retained earnings KShs'000	Proposed dividend KShs'000	Total equity KShs'000
At 1 January 2017		**3,411,549**	**3,444,639**	**65,597**	**(869,567)**	**44,672**	**122,598**	**13,861**	**22,604,133**	**1,400,000**	**30,237,482**
Profit for the year		-	-	-	-	-	-	-	4,339,136	-	**4,339,136**
Other comprehensive income, net of tax		-	-	-	73,788	298,645	-	-	-	-	**372,433**
Total comprehensive income for the year		**-**	**-**	**-**	**73,788**	**298,645**	**-**	**-**	**4,339,136**	**-**	**4,711,569**
Transfer from regulatory credit risk reserve	40	-	-	(65,524)	-	-	-	-	65,524	-	**-**
Transactions with owners recorded directly in equity											
Equity-settled share-based payment transactions	41	-	-	-	-	-	-	2,143	-	-	**2,143**
2017 Interim/ 2016 final dividend paid	18	-	-	-	-	-	-	-	(500,000)	(1,400,000)	**(1,900,000)**
2017 Final dividend proposed	18	-	-	-	-	-	-	-	(1,600,000)	1,600,000	**-**
Total transactions with owners		**-**	**-**	**-**	**-**	**-**	**-**	**2,143**	**(2,100,000)**	**200,000**	**(1,897,857)**
At 31 December 2017		**3,411,549**	**3,444,639**	**73**	**(795,779)**	**343,317**	**122,598**	**16,004**	**24,908,793**	**1,600,000**	**33,051,194**

The notes set out on pages 18 to 134 form an integral part of these financial statements.

Statement of cash flows

	Note	Year ended 31 December 2018 KShs'000	2017 KShs'000
Cash flows from operating activities	44.1	9,737,020	5,362,766
Income tax paid	33	(1,519,044)	(3,444,103)
Cash flows from operating activities before changes in operating assets and liabilities		**8,217,976**	**1,918,663**
Changes in operating assets and liabilities:			
Loans and advances to customers		(18,304,930)	(14,948,087)
Loans and advances to banks		1,749,076	(3,200,436)
Financial assets–held for trading		7,425,131	(13,336,722)
Financial assets – (FVOCI/available-for-sale)		23,739,044	1,686,998
Deposits held for regulatory purposes (restricted cash)		(4,676,580)	1,718,913
Other assets and prepayments		(84,354)	163,931
Amounts due to other banks		(12,161,298)	3,499,101
Other liabilities and accruals		353,812	(514,454)
Customer deposits		36,852,050	35,502,406
Trading liabilities		10,010,438	(3,505,088)
Net cash generated from operating activities		**53,120,365**	**8,985,225**
Cash flows from investing activities:			
Proceeds from sale of subsidiary		-	42,174
Financial investments – (amortised cost/held to maturity)		(17,756,778)	(5,444,178)
Purchase of property and equipment	30	(362,603)	(457,254)
Purchase of intangible assets - software	31	(144,686)	(436,543)
Proceeds from disposal of property and equipment		7,745	2,561
Net cash used in investing activities		**(18,256,322)**	**(6,293,240)**
Cash flows from financing activities:			
Dividends paid	18	(2,500,000)	(1,900,000)
Increase in borrowings		3,074,770	3,105
Net cash used in financing activities		**574,770**	**(1,896,895)**
Net increase in cash and cash equivalents		**35,438,813**	**795,090**
Cash and cash equivalents at start of year	44.2	25,796,368	24,881,380
Effect of exchange rate changes		(280,801)	119,898
Cash and cash equivalents at end of year	44.2	**60,954,380**	**25,796,368**

The notes set out on pages 18 to 134 form an integral part of these financial statements.

Notes

1 General information

Stanbic Bank Kenya Limited is incorporated in Kenya under the Companies Act as a limited liability company, and is domiciled in Kenya. The address of its registered office is:

Stanbic Bank Centre
Chiromo Road, Westlands
P.O. Box 72833
00200 Nairobi GPO

The Bank provides personal and business banking; corporate and investment banking services.

The financial statements for the year ended 31 December 2018 were approved for issue by the Board of Directors on 28 February 2019. Neither the entity's owners nor others have the power to amend the financial statements after issue.

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

2 Summary of significant accounting policies

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

a) Basis of preparation

The annual financial statements (AFS) are prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), its interpretations adopted by the IASB, and the Kenyan Companies Act. The annual financial statements have been prepared on the historical cost basis except for the following material items in the statement of financial position:

- Available-for-sale (FVOCI) financial assets, financial assets and liabilities at fair value through profit or loss and liabilities for cash-settled and equity-settled share-based payment arrangements (accounting policy 2.5).

The following principle accounting policy elections in terms of IFRS have been made, with reference to the detailed accounting policies shown in brackets:

- purchases and sales of financial assets under a contract whose terms require delivery of the asset within the time frame established generally by regulation or convention in the marketplace concerned are recognised and derecognised using trade date accounting (accounting policy 2.5);

- property and equipment and intangible assets are accounted for using the cost model except for revaluation of buildings that arose from the merger between CfC Bank and Stanbic Bank in 2008 (accounting policy 2.7 and 2.8);

- the portfolio exception to measure the fair value of certain groups of financial assets and financial liabilities on a net basis (accounting policy 2.6); and

- hyperinflation - the South Sudan economy has been considered to be hyperinflationary. Accordingly, the results, cash flows and financial position, have been expressed in terms of the measuring unit prevailing at the reporting date (accounting policy 2.21).

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires the directors to exercise judegment in applying the accounting policies.These judgements and estimates used to prepare these financial statements are disclosed in Note 3.

b) Functional and presentation currency

The annual financial statements are presented in Kenya Shillings (KShs) which is the functional and presentation currency of the Bank. All amounts are stated in thousands of shillings (KShs'000), unless indicated otherwise. Items included in the financial statements of each of the Bank's entities are measured using the currency of the primary economic environment in which the entity operates which is South Sudan Pound (SSP) for South Sudan operations and Kenya Shillings (KShs) for Kenya operations.

Notes (continued)

2 Summary of significant accounting policies (continued)

c) Changes in accounting policies and disclosures

(i) Standards and interpretations that have been published but are not yet effective

The Bank has not applied the following new and revised standard and interpretations that have been published but are not yet effective for the year beginning 1 January 2018.

IFRIC 23 - This Interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. In such a circumstance, an entity shall recognise and measure its current or deferred tax asset or liability applying the requirements in IAS 12 based on taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates determined applying this Interpretation. This Interpretation addresses: whether an entity considers uncertain tax treatments separately; the assumptions an entity makes about the examination of tax treatments by taxation authorities; how an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates; and how an entity considers changes in facts and circumstances. The IFRIC will be applied retrospectively. The new interpretation is effective on 1 January 2019 and earlier application is permitted. There are currently no uncertainties over tax treatments and therefore the impact of IFRIC 23 is not significant, at present.

IFRS 16- Leases This standard will replace the existing standard IAS 17 Leases as well as the related interpretations and sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, being the lessee (customer) and the lessor (supplier).

The core principle of this standard is that the lessee and lessor should recognise all rights and obligations arising from leasing arrangements on the statement of financial position.

The most significant change pertaining to the accounting treatment of operating leases is from the lessees' perspective. IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and introduces a single lessee accounting model, where a right of use (ROU) asset together with a liability for the future payments is to be recognised for all leases with a term of more than 12 months, unless the underlying asset is of low value.

The lessor accounting requirements in IAS 17 has not changed substantially in terms of this standard as a result a lessor continues to classify its leases as operating leases or finance leases and accounts for these as it currently done in terms of IAS 17. In addition, the standard requires lessor to provide enhanced disclosures about its leasing activities and in particular about its exposure to residual value risk and how it is managed.

The Bank has formed an IFRS 16 working group and detailed project plan, identifying key responsibilities and milestones of the project. The Bank is in the process of determining the estimated impact as well as discussing the system requirements to accommodate IFRS 16's principles. The new standard is effective on 1 January 2019 and earlier application is permitted. The impact is estimated to be a right of use asset of KShs 1.1 billion and a lease liability of the same amount.

Amendments to IFRS 9 titled Prepayment Features with Negative Compensation (issued in October 2017) - The amendments, applicable to annual periods beginning on or after 1 January 2019, allow entities to measure prepayable financial assets with negative compensation at amortised cost or fair value through other comprehensive income if a specified condition is met.

Amendments to IAS 12 - Annual Improvements to IFRSs 2015 – 2017 Cycle, issued in December 2017. The amendments, applicable to annual periods beginning on or after 1 January 2019, clarify that all income tax consequences of dividends should be recognised when a liability to pay a dividend is recognised, and that these income tax consequences should be recognised in profit or loss, other comprehensive income or equity according to where the entity originally recognised the transactions to which they are linked.

Amendments to IAS 23 - Annual Improvements to IFRSs 2015 – 2017 Cycle, issued in December 2017 The amendments, applicable to annual periods beginning on or after 1 January 2019, clarify that the costs of borrowings made specifically for the purpose of obtaining a qualifying asset that is substantially completed can be included in the determination of the weighted average of borrowing costs for other qualifying assets.

Notes (continued)

2 Summary of significant accounting policies (continued)

c) Changes in accounting policies and disclosures (continued)

(ii) Adoption of new and amended standards effective for the current period

Certain new accounting standards and interpretations were effective for the accounting period beginning on or after 1 January 2018. The Bank's assessment of the impact of these new standards and interpretations is set out below:

IFRS 15 Revenue from Contracts with Customers, with effect from 1 January 2018, replaces the existing revenue standards and the related interpretations. The standard sets out the requirements for recognising revenue that applies to all contracts with customers (except for contracts that are within the scope of the standards on leases, insurance contracts or financial instruments). The core principle of the standard is that revenue recognised reflects the consideration to which the company expects to be entitled in exchange for the transfer of promised goods or services to the customer. The standard incorporates a five step analysis to determine the amount and timing of revenue recognition. The Bank adopted IFRS 15 on 1 January 2018 and, as permitted by IFRS 15, did not restate its comparative financial results. The standard does not apply to revenue associated with financial instruments, and therefore does not impact the majority of the Bank's revenue. The Bank identified and reviewed its contracts with customers that are within the scope of IFRS 15 and concluded that adoption of this standard did not materially impact the Bank's revenue recognition. As such no transition adjustments were deemed necessary.

IFRIC 22 Foreign Currency Transactions and Advance Consideration provides guidance on how to determine 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) on the derecognition of a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration in a foreign currency. Management has performed an assessment of IFRIC 22 and the impact is not significant.

IFRS 2 (amendment) Share-based Payment: The amendments are intended to eliminate diversity in practice in three main areas of the classification and measurement of share- based payment transactions are:

- the effects of vesting conditions on the measurement of a cash-settled share based payment transaction; and

- the classification of a share-based payment transaction with net settlement features for withholding tax obligations the accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash-settled to equity-settled.

The amendments was applied prospectively on its effective date of 1 January 2018. Management has performed an assessment of IFRS 2 the impact is not significant.

IFRS 9 Financial instruments - The Bank adopted IFRS 9 as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which has resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements. The Bank did not early adopt any part of IFRS 9 in previous periods.

As permitted by the transitional provisions of IFRS 9, the Bank elected not to restate comparative figures. Adjustments to the carrying amounts of financial assets and liabilities at the date of transition were recognised in the opening retained earnings and other reserves of the current period.

Consequently, for notes disclosures, the consequential amendments to IFRS 7 disclosures have also been applied only to the current period. The comparative period notes disclosures repeat those disclosures made in the prior year.

The adoption of IFRS 9 has resulted in changes in the accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7, "*Financial Instruments: Disclosures*".

For more detail on IFRS 9 accounting policies see note 2.5.

Notes (continued)

2 Summary of significant accounting policies (continued)

c) Changes in accounting policies and disclosures (continued)

(ii) Adoption of new and amended standards effective for the current period (continued)

IFRS 9 key financial impacts

Table 1: Impact on the Bank's extracted statement of financial position on 1 January 2018:-

	IAS 39 at 31 December 2017	IFRS 9 transition adjustment at 1 January 2018: IFRS 9 ECL	IFRS 9 transition adjustment at 1 January 2018: IFRS 9 classification and measurements	IFRS 9 transition adjustment at 1 January 2018: Total	IFRS 9 at 1 January 2018
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Assets					
Financial investments	76,238,972	(17,849)	-	**(17,849)**	76,221,123
Loans and advances	143,176,319	(2,046,347)	-	**(2,046,347)**	141,129,971
Other financial and non financial assets	17,503,827	-	-	**-**	17,503,827
Deferred tax[1]	2,488,760	670,958	-	**670,958**	3,159,718
Total assets	**239,407,877**	**(1,393,238)**	**-**	**(1,393,238)**	**238,014,639**
Equity					
Odinary shares	(3,411,549)	-	-	**-**	(3,411,549)
Share premium	(3,444,639)	-	-	**-**	(3,444,639)
Other reserves	(481,919)	-	-	**-**	(481,919)
Retained earnings	(25,713,087)	1,565,567	-	**1,565,567**	(24,147,520)
Total equity	**(33,051,194)**	**1,565,567**	**-**	**1,565,567**	**(31,485,627)**
Liabilities[2]					
Other liabilities	(5,425,290)	(172,329)	-	**(172,329)**	(5,597,619)
All other liabilities	(200,931,393)	-	-	**-**	(200,931,393)
Total liabilities	**(206,356,683)**	**(172,329)**	**-**	**(172,329)**	**(206,529,012)**
Total equity and liabilities	**(239,407,877)**	**1,393,238**	**-**	**1,393,238**	**(238,014,639)**

[1] Materially relates to the recognition of additional deferred tax assets following the recognition of the IFRS 9 ECL transition adjustment.

[2] Materially relates to the recognition of ECL on off-balance sheet letters of credit, bankers acceptances and guarantees.

Table 2: Impact on the Bank's extracted statement of changes in equity on 1 January 2018:-

	IAS 39 at 31 December 2017	IFRS 9 transition adjustment at 1 January 2018	IFRS 9 at 1 January 2018
	KShs'000	KShs'000	KShs'000
Ordinary share capital and share premium	(6,856,188)	-	**(6,856,188)**
Retained earnings[1]	(25,713,087)	1,565,567	**(24,147,520)**
Other[2]	(481,919)	-	**(481,919)**
Total ordinary shareholder's equity	**(33,051,194)**	**1,565,567**	**(31,485,627)**

[1] The change in the retained earnings relates to IFRS 9's classification and measurement and ECL changes.

[2] This relates to release in the statutory reserve.

Notes (continued)

2 Summary of significant accounting policies (continued)

c) Changes in accounting policies and disclosures (continued)

(ii) Adoption of new and amended standards effective for the current period (continued)

IFRS 9 key financial impacts (continued)

Table 3: Impact on financial instrument classification (excluding impact of IFRS 9 ECL):-

		IFRS 9 transition adjustment at 1 January 2018				
	IAS 39 at 31 December 2017	Held-for-trading	Designated at fair value	Fair value through profit or loss - default	Amortised cost	Fair value through OCI
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Financial assets						
Cash and bank balances[1]	8,044,783	-	-	5,926,991	2,117,792	-
Held-for-trading	29,806,020	29,806,020	-	-	-	-
Available-for-sale	40,988,774	-	-	-	9,510,024	31,478,750
Held to maturity	5,444,178	-	-	-	5,444,178	-
Loans and receivables	143,176,320	-	-	3,096,666	139,054,336	-
Derivative assets	2,391,101	-	-	2,391,101	-	-
Other investments	17,500	-	-	17,500	-	-
Other assets	3,184,459	-	-	-	3,184,459	-
Total financial assets	**233,053,134**	**29,806,020**	**-**	**11,432,258**	**159,310,789**	**31,478,750**

[1] Cash and balances with central banks was in terms of IAS 39 classified as loans and receivables. Coins and bank notes and the reserving requirements held with the central bank have been classified as at fair value through profit or loss - default as the contractual terms do not give rise on specified dates to cash flows that represent solely payments of principal and interest on the principal amount outstanding.

The Bank applied IFRS 9's classification and measurement requirements based on the facts and circumstances at 1 January 2018 in determining the transition adjustment. As at 1 January 2018, the Bank determined the classification of financial assets on the basis of the business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. An assessment of the instrument's contractual terms was performed to determine whether the terms give rise on specified dates to cash flows that are solely payments of principal and interest of the principal amount outstanding (referred to as SPPI) and whether there is an accounting mismatch.

Equity financial assets are assessed to be designated as at fair value through profit or loss based on the facts and circumstances as at 1 January 2018.

Financial liabilities

From a classification perspective, with the exception of what is noted below, both IAS 39 and IFRS 9 have the same requirements for the classification of financial liabilities. From a recognition of gains and losses perspective, the amount of the change in fair value that is attributable to changes in the credit risk of financial liabilities that have been designated at fair value through profit and loss shall, in terms of IFRS 9, be recognised in OCI with the remaining amount of the change in the fair value of the financial liability being presented in profit or loss. The gains and losses presented in OCI are not subsequently recognised in profit or loss. Where, however, presenting the changes in the fair value of the liability due to changes in credit risk in OCI would create or enlarge an accounting mismatch in profit or loss, IFRS 9 permits the gains and losses due to changes in the credit risk of that liability to be recognised in profit or loss.

Notes (continued)

2 Summary of significant accounting policies (continued)

c) Changes in accounting policies and disclosures (continued)

(i) Adoption of new and amended standards effective for the current period (continued)

IFRS 9 key financial impacts (continued)

Table 4: The transition from IAS 39 to IFRS 9's impairment requirements by segment and asset class:-

	IAS 39 – 31 December 2017					IFRS 9 – 1 January 2018				IFRS 9 – transition adjustment		
	Performing portfolio provision	Specific debt provision	Total IAS 39 provision (excluding IIS)	IIS	Total IAS 39 provision (including IIS)	Stage 1	Stage 2	Stage 3	Total IFRS 9 provision (including IIS)	Gross	Tax	Net
	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000	Kshs'000
Personal & Business Banking	**378,864**	**1,632,282**	**2,011,146**	**503,267**	**2,514,413**	**307,778**	**1,260,333**	**1,632,282**	**3,703,660**	**1,189,247**	**356,774**	**832,473**
Loans and advances measured at amortised cost	**378,864**	**1,632,282**	**2,011,146**	**503,267**	**2,514,413**	**298,045**	**1,260,333**	**1,632,282**	**3,693,927**	**1,179,514**	**353,855**	**825,659**
Mortgage loans	122,694	250,748	373,441	208,988	582,429	15,476	178,453	250,748	653,664	71,235	21,371	49,864
Vehicle and asset finance	89,734	727,413	817,147	149,453	966,600	103,558	279,476	727,413	1,259,900	293,300	87,990	205,310
Card debtors	7,733	18,207	25,941	-	25,941	14,820	20,891	18,207	53,919	27,978	8,394	19,584
Other loans and advances	158,703	635,914	794,617	144,827	939,444	164,191	781,513	635,914	1,726,445	787,001	236,100	550,901
Off-balance sheet exposures	-	-	-	-	-	9,733	-	-	9,733	9,733	2,920	6,813
Corporate & Investment Banking	**1,641,541**	**1,611,318**	**3,252,859**	**1,160,705**	**4,413,564**	**488,799**	**2,139,318**	**1,672,019**	**5,460,842**	**1,047,278**	**314,184**	**733,094**
Loans and advances measured at amortised cost	**1,641,541**	**1,611,318**	**3,252,859**	**1,160,705**	**4,413,564**	**405,035**	**2,103,336**	**1,611,320**	**5,280,397**	**866,833**	**260,050**	**606,783**
Corporate	1,580,002	1,585,580	3,165,582	1,160,705	4,326,287	343,496	2,103,272	1,582,544	5,190,017	863,730	259,119	604,611
Sovereign	-	-	-	-	-	-	-	-	-	-	-	-
Bank	61,539	25,738	87,277	-	87,277	61,539	64	28,777	90,380	3,103	931	2,172
Debt financial investments measured at fair value through OCI	**-**	**-**	**-**	**-**	**-**	**2,859**	**-**	**-**	**2,859**	**2,859**	**858**	**2,001**
Sovereign	-	-	-	-	-	2,859	-	-	2,859	2,859	858	2,001
Debt financial investments measured at amortised cost	**-**	**-**	**-**	**-**	**-**	**11,791**	**3,199**	**-**	**14,990**	**14,990**	**4,497**	**10,493**
Corporate	-	-	-	-	-	528	-	-	528	528	158	370
Sovereign	-	-	-	-	-	11,263	3,199	-	14,462	14,462	4,339	10,123
Off-balance sheet exposures	**-**	**-**	**-**	**-**	**-**	**69,114**	**32,783**	**60,699**	**162,596**	**162,596**	**48,779**	**113,817**
Total	**2,020,405**	**3,243,600**	**5,264,005**	**1,663,972**	**6,927,977**	**796,577**	**3,399,652**	**3,304,301**	**9,164,502**	**2,236,525**	**670,958**	**1,565,567**

Notes (continued)

2 Summary of significant accounting policies (continued)

2.1 Translation of foreign currencies

(i) Functional and presentation currency

Items included in the Bank's financial statements are measured using the currency of the primary economic environment in which the entity operates ('the Functional Currency'), which is also the presentation currency.

(ii) Transactions and balances

Foreign currency transactions are translated into the respective Functional Currencies of bank entities at exchange rates prevailing at the date of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at year end exchange rates, are recognised in profit or loss (except when recognised in OCI as part of qualifying cash flow hedges and net investment hedges).

Non-monetary assets and liabilities denominated in foreign currencies that are measured at historical cost are translated using the exchange rate at the transaction date, and those measured at fair value are translated at the exchange rate at the date that the fair value was determined. Exchange rate differences on non-monetary items are accounted for based on the classification of the underlying items. Foreign exchange gains and losses on equities (debt) classified as available-for-sale financial assets are recognised in the available-for-sale reserve in OCI (profit or loss) whereas the exchange differences on equities and debt that are classified as held at fair value through profit or loss are reported as part of the fair value gain or loss in profit or loss.

(iii) Foreign operations

The results and financial position of our operations in South Sudan, which is a hyperinflationary economic environment and has a Functional Currency different from the Kenya Bank's presentation currency, are translated into Kenya Bank's presentation currency as follows:

- income and expenses are translated at average exchange rates for the month, to the extent that such average rates approximate actual rates for the transactions; and

- all resulting foreign exchange differences are accounted for directly in a separate component of OCI, being the foreign currency translation reserve.

On the partial disposal of a foreign operation, a proportionate share of the balance of the foreign currency translation reserve is transferred to the non-controlling interests. For all other partial disposals of a foreign operation, the proportionate share of the balance of the foreign currency translation reserve is reclassified to profit or loss.

On disposal (where a change in ownership occurs and control is lost) of a foreign operation, the relevant amount in the foreign currency translation reserve is reclassified to profit or loss at the time at which the profit or loss on disposal of the foreign operation is recognised.

These gains and losses are recognised in profit or loss either on disposal of a foreign operation or partial disposal (a reduction in ownership interest in a foreign operation other than a disposal) of an associate or joint venture that includes a foreign operation. In the case of a partial disposal of a foreign operation, the proportionate share of the cumulative amount of the exchange differences recognised in OCI is reclassified to the non-controlling interests in that foreign operation.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operation are translated at the closing rate. Exchange differences are recognised in OCI.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.2 Net interest income

Interest income and expense (with the exception of those borrowing costs that are capitalised – refer to accounting policy 2.9 – Capitalisation of borrowing costs) are recognised in profit or loss on an accrual basis using the effective interest method for all interest-bearing financial instruments, except for those classified at fair value through profit or loss which are included under trading income and:

a) purchased or originated credit impaired (POCI) for which the original credit adjusted effective interest rate is applied to the amortised cost of the financial asset; and

b) financial assets that are not "POCI" that have subsequently become impaired for which interest revenue is calculated by applying the effective interest rate to their amortised cost (i.e. net of expected credit losses) in subsequent reporting periods.

Effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial assets or, where appropriate,a shorter period to the net carrying amount of the financial asset or liability.

Direct incremental transaction costs incurred and origination fees received, including loan commitment fees, as a result of bringing margin-yielding assets or liabilities into the statement of financial position, are capitalised to the carrying amount of financial instruments that are not at fair value through profit or loss and amortised as interest income or expense over the life of the asset or liability as part of the effective interest rate.

Dividends received on preference share investments classified as debt form part of the Bank's lending activities and are included in interest income.

2.3 Non-interest revenue

a) Net fee and commission revenue

Fee and commission revenue, including transactional fees, account servicing fees, investment management fees, sales commissions and placement fees are recognised as the related services are performed. Loan commitment fees for loans that are not expected to be drawn down are recognised on a straight-line basis over the commitment period. Loan syndication fees, where the Bank does not participate in the syndication or participates at the same effective interest rate for comparable risk as other participants, are recognised as revenue when the syndication has been completed. Syndication fees that do not meet these criteria are capitalised as origination fees and amortised as interest income.

The fair value of issued financial guarantee contracts on initial recognition is amortised as income over the term of the contract.

Fee and commission expense included in net fee and commission revenue are mainly transaction and service fees relating to financial instruments, which are expensed as the services are received. Expenditure is recognised as fee and commission expenses where the expenditure is linked to the production of fee and commission revenue.

b) Trading revenue

Trading revenue comprises all gains and losses from changes in the fair value of trading assets and liabilities, together with related interest income, expense and dividends.

c) Other

Other revenue includes gains and losses on equity instruments designated at fair value through profit or loss, dividends relating to those financial instruments, and remeasurement gains and losses from contingent consideration on disposals and purchases.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.3 Non-interest revenue (continued)

d) Revenue sharing agreements with related companies

Revenue sharing agreements with related companies includes the allocation of revenue from transfer pricing agreements between the group's legal entities. The service payer makes payment to service sellers for services rendered. All agreements of a revenue sharing nature are presented in the income statement as follows:

- The service payer of the agreement recognises, to the extent the charge is less than revenue from the agreement, the charge to the service sellers within the income statement line item revenue sharing agreements with related companies. To the extent that the revenue allocation to service sellers within the group is greater than the available revenue from the agreement, the charge above the available revenue is recognised within other operating expenses.

- The service seller of the agreements recognises, to the extent the allocation is made out of available revenue of the service payer, the revenue from the service payer within the income statement line item revenue sharing agreements with related companies. To the extent the revenue is not received from the service payer's available revenue, such revenue is recognised as a fee and commission revenue.

2.4 Cash and cash equivalents

Cash and cash equivalents as referred to in the cash flow statement comprises cash on hand, non–restricted balances with central banks, Treasury and other eligible bills and amounts due from banks on demand or with an original maturity of three months or less. These are subject to insignificant risk of changes in their fair value.

2.5 Financial instruments

(i) Initial recognition and measurement

(IFRS 9 and IAS 39)

All financial instruments are measured initially at fair value plus directly attributable transaction costs and fees, except for those financial instruments that are subsequently measured at fair value through profit or loss where such transaction costs and fees are immediately recognised in profit or loss. Financial instruments are recognised (derecognised) on the date the Bank commits to purchase (sell) the instruments (trade date accounting).

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IFRS 9 - accounting policies for financial instruments

Financial assets

Nature	
Amortised cost	A debt instrument that meets both of the following conditions (other than those designated at fair value through profit or loss): ● held within a business model whose objective is to hold the debt instrument (financial asset) in order to collect contractual cash flows; and ● The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. This assessment includes determining the objective of holding the asset and whether the contractual cash flows are consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are not considered de minimis and are inconsistent with a basic lending arrangement, the financial asset is classified as fair value through profit or loss - default.
Fair value through OCI	A debt instrument that meets both of the following conditions (other than those designated at fair value through profit or loss): ● Held within a business model in which the debt instrument (financial asset) is managed to both collect contractual cash flows and sell financial assets; and ● The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. This assessment includes determining the objective of holding the asset and whether the contractual cash flows are consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are not considered de minimis and are inconsistent with a basic lending arrangement, the financial asset is classified as fair value through profit or loss - default. Equity financial assets which are not held for trading and are irrevocably elected (on an instrument-by-instrument basis) to be presented at fair value through OCI.
Held for trading	Those financial assets acquired principally for the purpose of selling in the near term (including all derivative financial assets) and those that form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking.
Designated at fair value through profit or loss	Financial assets are designated to be measured at fair value to eliminate or significantly reduce an accounting mismatch that would otherwise arise.
Fair value through profit or loss - default	Financial assets that are not classified into one of the above mentioned financial asset categories.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IFRS 9 - accounting policies for financial instruments (continued)

Financial assets (continued)

(ii) Subsequent measurement

Subsequent to initial measurement, financial instruments are measured either at fair value or amortised cost, depending on their classifications as follows:

Amortised cost	Amortised cost using the effective interest method with interest recognised in interest income, less any expected credit impairment losses which are recognised as part of credit impairment charges.
	Directly attributable transaction costs and fees received are capitalised and amortised through interest income as part of the effective interest rate.
Fair value through OCI	Debt instrument: Fair value, with gains and losses recognised directly in the fair value through OCI reserve. When a debt financial asset is disposed of, the cumulative fair value adjustments, previously recognised in OCI, are reclassified to the other gains and losses on financial instruments within non-interest revenue.
	Interest income on a debt financial asset is recognised in interest income in terms of the effective interest rate method. Dividends received are recognised in interest income within profit or loss.
	Dividends received on equity instruments are recognised in other revenue within non-interest income.
Held for trading	Fair value, with gains and losses arising from changes in fair value (including interest and dividends) recognised in trading revenue.
Designated at fair value through profit or loss	Fair value gains and losses (including interest and dividends) on the financial asset are recognised in the income statement as part of other gains and losses on financial instruments within non-interest revenue.
Fair value through profit or loss - default	Fair value gains and losses (including interest and dividends) on the financial asset are recognised in the income statement as part of other gains and losses on financial instruments within non-interest revenue.

Impairment of financial assets

Expected credit losses (ECL) are recognised on debt financial assets classified as at either amortised cost or fair value through OCI, financial guarantee contracts that are not designated at fair value through profit or loss as well as loan commitments that are neither measured at fair value through profit or loss nor are used to provide a loan at a below market interest rate.

The measurement basis of the ECL of a financial asset includes assessing whether there has been a Significant Increase in Credit Risk (SICR) at the reporting date which includes forward-looking information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions. The measurement basis of the ECL, which is set out in the table that follows, is measured as the unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes, the time value of money and forward-looking information.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IFRS 9 - accounting policies for financial instruments (continued)

Financial assets (continued)

Impairment (continued)

Stage 1	A 12-month ECL is calculated for financial assets which are neither credit-impaired on origination nor for which there has been a SICR.
Stage 2	A lifetime ECL allowance is calculated for financial assets that are assessed to have displayed a SICR since origination and are not considered low credit risk.
Stage 3 (credit impaired assets)	A lifetime ECL is calculated for financial assets that are assessed to be credit impaired. The following criteria are used in determining whether the financial asset is impaired: ● default; ● significant financial difficulty of borrower and/or modification; ● probability of bankruptcy or financial reorganisation; and ● disappearance of an active market due to financial difficulties.

The key components of the impairment methodology are described as follows:

Significant increase in credit risk	At each reporting date the Bank assesses whether the credit risk of its exposures has increased significantly since initial recognition by considering the change in the risk of default occurring over the expected life of the financial asset.
Low credit risk	Exposures are generally considered to have a low credit risk where there is a low risk of default, the exposure has a strong capacity to meet its contractual cash flow obligations and adverse changes in economic and business conditions may not necessarily reduce the exposure's ability to fulfil its contractual obligations.
Default	The Bank's definition of default has been aligned to its internal credit risk management definitions and approaches. A financial asset is considered to be in default when there is objective evidence of impairment. The following criteria are used in determining whether there is objective evidence of impairment for financial assets or groups of financial assets: ● significant financial difficulty of borrower and/or modification (i.e. known cash flow difficulties experienced by the borrower); ● a breach of contract, such as default or delinquency in interest and/or principal payments; ● disappearance of active market due to financial difficulties; ● it becomes probable that the borrower will enter bankruptcy or other financial reorganisation; ● where the Bank, for economic or legal reasons relating to the borrower's financial difficulty, grants the borrower a concession that the Bank would not otherwise consider; ● Exposures which are overdue for more than 90 days are also considered to be in default.
Forward-looking information	Forward-looking information is incorporated into the Bank's impairment methodology calculations and in the Bank's assessment of SICR. The Bank includes all forward looking information which is reasonable and available without undue cost or effort. The information will typically include expected macro-economic conditions and factors that are expected to impact portfolios or individual counterparty exposures.
Write-off	Financial assets are written off when there is no reasonable expectation of recovery. Financial assets which are written off may still be subject to enforcement activities.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IFRS 9 - accounting policies for financial instruments (continued)

Financial assets (continued)

ECLs are recognised within the statement of financial position as follows:

Financial assets measured at amortised cost (including loan commitments)	Recognised as a deduction from the gross carrying amount of the asset (group of assets). Where the impairment allowance exceeds the gross carrying amount of the asset (group of assets), the excess is recognised as a provision within other liabilities.
Off-balance sheet exposures (excluding loan commitments)	Recognised as a provision within other liabilities.
Financial assets measured at fair value through OCI	Recognised in the fair value reserve within equity. The carrying value of the financial asset is recognised in the statement of financial position at fair value.

Reclassification

Reclassifications of debt financial as sets are permitted when, and only when, the Bank changes its business model or managing financial assets, in which case all affected financial assets are reclassified. Reclassifications are accounted for prospectively from the date of reclassification as follows:

- Financial assets that are reclassified from amortised cost to fair value are measured at fair value at the date of reclassification with any difference in measurement basis being recognised in other gains and losses on financial instruments;
- The fair value of a financial asset that is reclassified from fair value to amortised cost becomes the financial asset's new carrying value;
- Financial assets that are reclassified from amortised cost to fair value through OCI are measured at fair value at the date of reclassification with any difference in measurement basis being recognised in OCI;
- The fair value of a financial asset that is reclassified from fair value through OCI to amortised cost becomes the financial asset's new carrying value with the cumulative fair value adjustment recognised in OCI being recognised against the new carrying value;
- The carrying value of financial assets that are reclassified from fair value through profit or loss to fair value through OCI remains at fair value;
- The carrying value of financial assets that are reclassified from fair value through OCI to fair value through profit or loss remains at fair value, with the cumulative fair value adjustment in OCI being recognised in the income statement at the date of reclassification.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IFRS 9 - accounting policies for financial instruments (continued)

Financial liabilities

Nature	
Held-for-trading	Those financial liabilities incurred principally for the purpose of repurchasing in the near term (including all derivative financial liabilities) and those that form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking.
Designated at fair value through profit or loss	Financial liabilities are designated to be measured at fair value in the following instances to eliminate or significantly reduce an accounting mismatch that would otherwise arise where; ● the financial liabilities are managed and their performance evaluated and reported on a fair value basis; and ● the financial liability contains one or more embedded derivatives that significantly modify the financial liabilty's cash flows.
Amortised cost	All other financial liabilities not included in the above categories.

Subsequent measurement

Subsequent to initial measurement, financial liabilities are classified in their respective categories and measured at either amortised cost or fair value as follows:

Held-for-trading	Fair value, with gains and losses arising from changes in fair value (including interest and dividends) recognised in trading revenue.
Designated at fair value through profit or loss	Fair value, with gains and losses arising from changes in fair value (including interest and dividends but excluding fair value gains and losses attributable to own credit risk) are recognised in the other gains and losses on financial instruments as part of non-interest Fair value gains and losses attributable to changes in own credit risk are recognised within OCI, unless this would create or enlarge an accounting mismatch in which case the own credit risk changes are recognised within trading revenue.
Amortised cost	Amortised cost using the effective interest method recognised in interest expense.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IFRS 9 - accounting policies for financial instruments (continued)

Derecognition and modification of financial assets and liabilities

Financial assets and liabilities are derecognised in the following instances:

<table>
<tr><th></th><th>DERECOGNITION</th><th>MODIFICATION</th></tr>
<tr><td rowspan="3">Financial assets</td><td>Financial assets are derecognised when the contractual rights to receive cash flows from the financial assets have expired, or where the Bank has transferred its contractual rights to receive cash flows on the financial asset such that it has transferred substantially all the risks and rewards of ownership of the financial asset. Any interest in the transferred financial assets that is created or retained by the Bank is recognised as a separate asset or liability.</td><td rowspan="2">Where an existing financial asset or liability is replaced by another with the same counterparty on substantially different terms, or the terms of an existing financial asset or liability are substantially modified, such an exchange or modification is treated as a derecognition of the original asset or liability and the recognition of a new asset or liability at fair value, including calculating a new effective interest rate, with the difference in the respective carrying amounts being recognised in other gains and losses on financial instruments within non-interest revenue. The date of recognition of a new asset is consequently considered to be the date of initial recognition for impairment calculation purposes.</td></tr>
<tr><td>The Bank enters into transactions whereby it transfers assets, recognised in its statement of financial position, but retains either all or a portion of the risks or rewards of the transferred assets. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised. Transfers of assets with the retention of all or substantially all risks and rewards include securities lending and repurchase agreements.</td></tr>
<tr><td>When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction, similar to repurchase transactions. In transactions where the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset, the asset is derecognised if control over the asset is lost. The rights and obligations retained in the transfer are recognised separately as assets and liabilities as appropriate.
In transfers where control over the asset is retained, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.</td><td>If the terms are not substantially different for financial assets or financial liabilities, the Bank recalculates the new gross carrying amount by discounting the modified cash flows of the financial asset or financial liability using the original effective interest rate. The difference between the new gross carrying amount and the original gross carrying amount is recognised as a modification gain or loss within credit impairments (for distressed financial asset modifications) or in other gains and losses on financial instruments within non-interest revenue (for all other modifications).</td></tr>
<tr><td>Financial liabilities</td><td>Financial liabilities are derecognised when the financial liabilities' obligation is extinguished, that is, when the obligation is discharged, cancelled or expires.</td><td></td></tr>
</table>

Financial guarantee contracts

A financial guarantee contract is a contract that requires the Bank (issuer) to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

Financial guarantee contracts are initially recognised at fair value, which is generally equal to the premium received, and then amortised over the life of the financial guarantee. Financial guarantee contracts (that are not designated at fair value through profit or loss) are subsequently measured at the higher of the:

- ECL calculated for the financial guarantee; or
- unamortised premium.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IAS 39 - Accounting Policies for financial instruments

The IAS 39 related accounting policies below are provided because financial instruments comparative balances were recognised and measured under this standard.

Subsequent measurement

Subsequent to initial measurement, financial instruments are measured either at fair value or amortised cost, depending on their classifications as follows:

(a) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that management has both the positive intention and ability to hold to maturity. This excludes:

1) those that the Bank upon initial recognition designates at fair value through profit or loss;
2) those the Bank designates as available for sale; and
3) those that meet the definition of loans and receivables.

Held-to-maturity investments are carried at amortised cost, using the effective interest method, less any impairment losses.

(b) Held-for-trading assets and liabilities

Held-for-trading assets and liabilities include those financial assets and liabilities acquired or incurred principally for the purpose of selling or repurchasing in the near term, those forming part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking, and commodities that are acquired principally by the Bank for the purpose of selling in the near future and generating a profit from fluctuations in price or broker-traders' margin. Derivatives are always categorised as held-for-trading.

Subsequent to initial recognition, the financial instruments' fair values are remeasured at each reporting date. All gains and losses, including interest and dividends arising from changes in fair value are recognised in profit or loss as trading revenue within non-interest revenue with the exception of derivatives that are designated and effective as hedging instruments (refer to note 2.5 (c).

(c) Financial assets and liabilities designated at fair value through profit or loss

The Bank designates certain financial assets and liabilities, other than those classified as held-for-trading, as at fair value through profit or loss when:

- this designation eliminates or significantly reduces an accounting mismatch that would otherwise arise. Under this criterion, the main classes of financial instruments designated by the Bank are loans and advances to banks and customers and financial investments. The designation significantly reduces measurement inconsistencies that would have otherwise arisen. For example, where the related derivatives were treated as held-for-trading and the underlying financial instruments were carried at amortised cost. This category also includes financial assets used to match investment contracts;

- groups of financial assets, financial liabilities or both are managed, and their performance evaluated, on a fair value basis in accordance with a documented risk management or investment strategy, and reported to the bank's key management personnel on a fair-value basis. Under this criterion, certain private equity, and other investment portfolios have been designated at fair value through profit or loss; or

- financial instruments containing one or more embedded derivatives that significantly modify the instruments' cash flows. Subsequent to initial recognition, the fair values are remeasured at each reporting date. Gains and losses arising from changes in fair value are recognised in interest income (interest expense) for all debt financial assets (financial liabilities) and in other revenue within non-interest revenue for all equity instruments.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IAS 39 - Accounting Policies for financial instruments (continued)

Subsequent measurement (continued)

(d) Available-for-sale

Financial assets classified by the Bank as available-for-sale are generally strategic capital investments held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices, or non-derivative financial assets that are not classified within another category of financial assets.

Available-for-sale financial assets are subsequently measured at fair value. Unrealised gains or losses are recognised directly in the available-for-sale reserve until the financial asset is derecognised or impaired. When debt or equity available-for-sale financial assets are disposed of, the cumulative fair value adjustments in OCI are reclassified to interest income.

Available-for-sale financial assets are impaired when there has been a significant or prolonged decline in the fair value of the financial asset below its cost. The cumulative fair value adjustments previously recognised in OCI on the impaired financial assets are reclassified to profit or loss. Reversals of impairments on equity available-for-sale financial assets are recognised in OCI.

Interest income, calculated using the effective interest method, is recognised in profit or loss. Dividends received on equity available-for-sale instruments are recognised in other revenue within profit or loss when the Bank’s right to receive payment has been established.

(e) Loans and advances

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those classified by the bank as at fair value through profit or loss or available-for-sale.

Loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses. Origination transaction costs and origination fees received that are integral to the effective rate are capitalised to the value of the loan and amortised through interest income as part of the effective interest rate. The majority of the Bank’s loans and advances are included in the loans and receivables category.

(f) Financial liabilities at amortised cost

Financial liabilities that are neither held for trading nor designated at fair value are measured at amortised cost.

Reclassification of financial assets

The Bank may choose to reclassify non-derivative trading assets out of the held-for-trading category if the financial asset is no longer held for the purpose of selling it in the near term. Financial assets that would not otherwise have met the definition of loans and receivables are permitted to be reclassified out of the held-for-trading category only in rare circumstances. In addition, the Bank may choose to reclassify financial assets that would meet the definition of loans and receivables out of the held-for-trading or available-for-sale categories if the Bank, at the date of reclassification, has the intention and ability to hold these financial assets for the foreseeable future or until maturity.

Derivatives or any financial instrument designated at fair value through profit or loss shall not be reclassified out of their respective categories.

Reclassifications are made at fair value as of the reclassification date. Effective interest rates for financial assets reclassified to loans and receivables, held-to-maturity and available-for-sale categories are determined at the reclassification date. Subsequent increases in estimates of cash flows adjust the financial asset’s effective interest rates prospectively.

On reclassification of a trading asset, all embedded derivatives are reassessed and, if necessary, accounted for separately.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IAS 39 - Accounting Policies for financial instruments (continued)

Impairment of financial assets

a) Assets carried at amortised cost

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is impaired if objective evidence indicates that a loss event has occurred after initial recognition which has a negative effect on the estimated future cash flows of the loan or group of loans that can be estimated reliably.

Criteria that are used by the bank in determining whether there is objective evidence of impairment include:

- known cash flow difficulties experienced by the borrower;
- a breach of contract, such as default or delinquency in interest and/or principal payments;
- breaches of loan covenants or conditions;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganisation, and
- where the Bank, for economic or legal reasons relating to the borrower's financial difficulty, grants the borrower a concession that the Bank would not otherwise consider.

The Bank first assesses whether there is objective evidence of impairment individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Non-performing loans include those financial assets for which the Bank has identified objective evidence of default, such as a breach of a material financial asset, covenant or condition as well as those loans for which instalments are due and unpaid for 90 days or more. The impairment of non-performing loans takes into account past loss experience adjusted for changes in economic conditions and the nature and level of risk exposure since the recording of the historic losses.

When a financial asset carried at amortised cost has been identified as specifically impaired, the carrying amount of the financial asset is reduced to an amount equal to the present value of its estimated future cash flows, including the recoverable amount of any collateral, discounted at the financial asset's original effective interest rate. The carrying amount of the loan is reduced through the use of a specific credit impairment account and the loss is recognised as a credit impairment charge in profit or loss.

The calculation of the present value of the estimated future cash flows of collateralised financial assets recognised on an amortised cost basis includes cash flows that may result from foreclosure less costs of obtaining and selling the collateral, whether or not foreclosure is probable.

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

Impairment of groups of financial assets that are assessed collectively is recognised where there is objective evidence that a loss event has occurred after the initial recognition of the group of loans but before the reporting date. In order to provide for latent losses in a group of loans that have not yet been identified as specifically impaired, a credit impairment for incurred but not reported losses is recognised based on historic loss patterns and estimated emergence periods (time period between the loss trigger events and the date on which the bank identifies the losses). Groups of financial assets are also impaired when adverse economic conditions develop after initial recognition, which may impact future cash flows. The carrying amount of groups of loans is reduced through the use of a portfolio credit impairment account and the loss is recognised as a credit impairment charge in statement of comprehensive income.

Increases in financial assets and any subsequent reversals thereof, or recoveries of amounts previously impaired (including loans that have been written off), are reflected within credit impairment charges in profit or loss. Previously impaired financial assets are written off once all reasonable attempts at collection have been made and there is no realistic prospect of recovering outstanding amounts. Any subsequent reductions in amounts previously impaired are reversed by adjusting the allowance account with the amount of the reversal recognised as a reduction in impairment for credit losses in profit or loss.

Subsequent to impairment, the effects of discounting unwind over time as interest income.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IAS 39 - Accounting Policies for financial instruments (continued)

Impairment of financial assets (continued)

b) Renegotiated loans

Loans that would otherwise be past due or impaired and whose terms have been renegotiated and exhibit the characteristics of a performing loan are reset to performing loan status. Loans whose terms have been renegotiated are subject to on-going review to determine whether they are considered to be impaired or past due.

The effective interest rate of renegotiated loans that have not been derecognised (described under the heading Derecognition of financial instruments), is predetermined based on the loan's renegotiated terms.

c) Available-for-sale financial assets

Available-for-sale financial assets are impaired if there is objective evidence of impairment, resulting from one or more loss events that occurred after initial recognition but before the reporting date, that have a negative impact on the future cash flows of the asset. In addition, an available-for-sale equity instrument is considered to be impaired if a significant or prolonged decline in the fair value of the instrument below its cost has occurred. In that instance, the cumulative loss, measured as the difference between the acquisition price and the current fair value, less any previously recognised impairment losses on that financial asset, is reclassified from OCI to profit or loss.

If, in a subsequent period, the amount relating to impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss for available-for-sale debt instruments. Any reversal of an impairment loss in respect of an available-for-sale equity instrument is recognised directly in OCI.

Borrowings

Borrowings are recognised initially at fair value, generally being their issue proceeds, net of directly attributable transaction costs incurred. Borrowings are subsequently measured at amortised cost and interest is recognised using the effective interest method.

Financial guarantee contracts

A financial guarantee contract is a contract that requires the Bank (issuer) to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

Financial guarantee contracts are initially recognised at fair value, which is generally equal to the premium received, and then amortised over the life of the financial guarantee. Subsequent to initial recognition, the financial guarantee liability is measured at the higher of the present value of any expected payment, when a payment under the guarantee has become probable, and the unamortised premium.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IAS 39 - Accounting Policies for financial instruments (continued)

Derecognition of financial instruments

Financial assets are derecognised when the contractual rights to receive cash flows from the financial assets have expired, or where the Bank has transferred its contractual rights to receive cash flows on the financial asset such that it has transferred substantially all the risks and rewards of ownership of the financial asset. Any interest in transferred financial assets that is created or retained by the bank is recognised as a separate asset or liability.

The Bank enters into transactions whereby it transfers assets recognised in its statement of financial position, but retains either all or a portion of the risks or rewards of the transferred assets. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised. Transfers of assets with the retention of all or substantially all risks and rewards include securities lending and repurchase agreements. When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction, similar to repurchase transactions. In transactions where the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset, the asset is derecognised if control over the asset is lost. The rights and obligations retained in the transfer are recognised separately as assets and liabilities as appropriate. In transfers where control over the asset is retained, the bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset. Financial liabilities are derecognised when they are extinguished, that is, when the obligation is discharged, cancelled or expires.

Where an existing financial asset or liability is replaced by another with the same counterparty on substantially different terms, or the terms of an existing financial asset or liability are substantially modified, such an exchange or modification is treated as a derecognition of the original asset or liability and the recognition of a new asset or liability, with the difference in the respective carrying amounts being recognised in profit or loss.

In all other instances, the renegotiated asset or liability's effective interest rate is predetermined taking into account the renegotiated terms.

Derivative and embedded derivatives (IFRS 9 and IAS 39)

A derivative is a financial instrument whose fair value changes in response to an underlying variable, requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors and is settled at a future date.

In the normal course of business, the Bank enters into a variety of derivative transactions for both trading and hedging purposes. Derivative financial instruments are entered into for trading purposes and for hedging foreign exchange, interest rate, inflation, credit, commodity and equity exposures. Derivative instruments used by the Bank in both trading and hedging activities include swaps, options, forwards, futures and other similar types of instruments based on foreign exchange rates, credit risk, inflation risk, interest rates and the prices of commodities and equities.

Derivatives are initially recognised at fair value. Derivatives that are not designated in a qualifying hedge accounting relationship are classified as held-for-trading with all changes in fair value being recognised within trading revenue. This includes forward contracts to purchase or sell commodities, where net settlement occurs or where physical delivery occurs and the commodities are held to settle another derivative contract. All derivative instruments are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

In terms on IFRS 9 embedded derivatives included in hybrid instruments, where the host is a financial asset, is assessed in terms of the accounting policy on financial assets. In all other instances (being non-financial host contracts and financial liabilities), the embedded derivatives are treated and disclosed as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract, the terms of the embedded derivative are the same as those of a stand-alone derivative and the combined contract is not measured at fair value through profit or loss. The host contract is accounted for and measured applying the relevant Bank accounting policy.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.5 Financial instruments (continued)

IAS 39 - Accounting Policies for financial instruments (continued)

Derivative and embedded derivatives (IFRS 9 and IAS 39) (continued)

In terms of IAS 39 Embedded derivatives included in hybrid instruments are treated and disclosed as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract, the terms of the embedded derivative are the same as those of a stand-alone derivative and the combined contract is not measured at fair value through profit or loss. The host contract is accounted for and measured applying the relevant Bank accounting policy.

The method of recognising fair value gains and losses on derivatives designated as a hedging instrument depends on the nature of the hedge relationship.

Sale and repurchase agreements and lending of securities

Securities sold subject to linked repurchase agreements (Repos) are reclassified in the statement of financial position as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral. The liability to the counterparty is included under deposit and current accounts or trading liabilities, as appropriate.

Securities purchased under agreements to resell (reverse repurchase agreements), at either a fixed price or the purchase price plus a lender’s rate of return, are recorded as loans and included under trading assets or loans and advances, as appropriate.

For repurchase and reverse repurchase agreements measured at amortised cost, the difference between the purchase and sales price is treated as interest and amortised over the expected life using the effective interest method.

Securities lent to counterparties are retained in the annual financial statements. Securities borrowed are not recognised in the annual financial statements unless sold to third parties. In these cases, the obligation to return the securities borrowed is recorded at fair value as a trading liability.

Income and expenses arising from the securities borrowing and lending business are recognised over the period of the transactions.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set-off the recognised amounts and there is an intention to settle the asset and the liability 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 by the accounting standards, or for gains and losses arising from a group of similar transactions.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.6 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 in the principal (or most advantageous) market between market participants at the measurement date under current market conditions.

When a price for an identical asset or liability is not observable, fair value is measured using another valuation technique that maximises the use of relevant observable inputs and minimises the use of unobservable inputs.

In estimating the fair value of an asset or a liability, the Bank takes into account the characteristics of the asset or liability that market participants would take into account when pricing the asset or liability at measurement date.

For financial instruments, where the fair value of the financial instrument differs from the transaction price, the difference is commonly referred to as day one profit or loss. Day one profit or loss is recognised in profit or loss immediately where the fair value of the financial instrument is either evidenced by comparison with other observable current market transactions in the same instrument, or is determined using valuation models with only observable market data as inputs.

Day one profit or loss is deferred where the fair value of the financial instrument is not able to be evidenced by comparison with other observable current market transactions in the same instrument, or determined using valuation models that utilise non-observable market data as inputs. The timing of the recognition of deferred day one profit or loss is determined individually depending on the nature of the instrument and availability of market observable inputs. It is either amortised over the life of the transaction, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

Subsequent to initial recognition, fair value is measured based on quoted market prices or dealer price quotations for the assets and liabilities that are traded in active markets and where those quoted prices represent fair value at the measurement date.

If the market for an asset or liability is not active or the instrument is unlisted, the fair value is determined using other applicable valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analyses, pricing models and other valuation techniques commonly used by market participants.

Where discounted cash flow analyses are used, estimated future cash flows are based on management's best estimates and a market related discount rate at the reporting date for an asset or liability with similar terms and conditions.

If an asset or a liability measured at fair value has both a bid and an ask price, the price within the bid-ask spread that is most representative of fair value is used to measure fair value.

The Bank has elected the portfolio exception to measure the fair value of certain groups of financial assets and financial liabilities. This exception permits a group of financial assets and financial liabilities to be measured at fair value on a net basis. This election is applied where the Bank:

- manages the group of financial assets and financial liabilities on the basis of the Bank's net exposure to a particular market risk (or risks) or to the credit risk of a particular counterparty in accordance with the Bank's documented risk management or investment strategy;
- provides information on that basis about the group of financial assets and financial liabilities to the bank's key management personnel; and
- is required to or has elected to measure those financial assets and financial liabilities at fair value at the end of each reporting period.

Fair value measurements are categorised into level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.7 Property and equipment

Equipment and owner-occupied properties, furniture, vehicles and other tangible assets are measured at cost less accumulated depreciation and accumulated impairment losses, if any.

Cost includes expenditure that is directly attributable to the acquisition of the asset. Where significant parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment. Costs that are subsequently incurred are included in the asset's related carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits will flow to the bank and the cost of the item can be measured reliably. Expenditure, which does not meet these criteria, is recognised the income statement as incurred.

Owner-occupied properties are held for use in the supply of services or for administrative purposes.

Property and equipment are depreciated on the straight-line basis over the estimated useful lives of the assets to their residual values. Land is not depreciated. Leasehold buildings are depreciated over the shorter of the lease period or its useful life.

The revaluation reserve in equity arose from revaluation of the Stanbic Bank, Chiromo Road office at the point where CfC Bank and Stanbic Bank merged.

The estimated useful lives of tangible assets are typically as follows;

Buildings	40 years
Motor vehicles	4-5 years
Computer equipment	3-5 years
Office equipment	5-10 years
Furniture and fittings	5-13 years
Capitalised leased	over the shorter of the lease term or its useful life

There has been no significant change to the estimated useful lives and depreciation methods from those applied in the previous financial year.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognising of the item is included in the income statement in the year the asset is derecognised.

The assets' residual values, useful lives and the depreciation method applied are reviewed, and adjusted if appropriate, at each financial year end.

2.8 Intangible assets – computer software

Costs associated with developing or maintaining computer software programmes and the acquisition of software licences are generally recognised as an expense as incurred. However, direct computer software development costs that are clearly associated with an identifiable and unique system, which will be controlled by the bank and have a probable future economic benefit beyond one year, are recognised as intangible assets. Capitalisation is further limited to development costs where the bank is able to demonstrate its intention and ability to complete and use the software, the technical feasibility of the development, and the availability of resources to complete the development, how the development will generate probable future economic benefits and the ability to reliably measure costs relating to the development. Direct costs include software development employee costs and an appropriate portion of relevant overheads.

Expenditure subsequently incurred on computer software is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. Development costs previously recognised as an expense are not recognised as an asset in subsequent periods.

Direct computer software development costs recognised as intangible assets are amortised on the straight-line basis at rates appropriate to the expected useful lives of the assets (2 to 10 years) from the date that the assets are available for use, and are carried at cost less accumulated amortisation and accumulated impairment losses. The carrying amount of capitalised computer software is reviewed annually and is written down when impaired.

Amortisation methods, useful lives and residual values are reviewed at each financial year end and adjusted, if

Notes (continued)

2 Summary of significant accounting policies (continued)

2.9 Capitalisation of borrowing costs

Borrowing costs that relate to qualifying assets, that is, assets that necessarily take a substantial period of time to get ready for their intended use or sale and which are not measured at fair value, are capitalised. All other borrowing costs are recognised in profit or loss. Borrowing costs consist of interest and other costs that an entity incurred in connection with the borrowing of funds.

2.10 Impairment of non-financial assets

Non-financial assets are tested annually for impairment and additionally whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised in profit or loss for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Fair value less costs to sell is determined by ascertaining the current market value of an asset and deducting any costs related to the realisation of the asset. 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. For the purposes of assessing impairment, assets that cannot be tested individually are grouped at the lowest levels for which there are separately identifiable cash inflows from continuing use (CGUs).Impairment test also can be performed on a single asset when the fair value less costs to sell or the value in use can be determined reliably. 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 through profit or loss 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.

Further disclosures relating to impairment of non-financial assets are also provided in the following notes:

- Property and equipment see note 30, note 2.7
- Intangible assets see note 31, note 2.8
- Disclosure on significant assumptions see note 3

2.11 Leases

A lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.

A lease of assets is either classified as a finance lease or operating lease.

(i) Bank as lessee

Leases, where the Bank assumes substantially all the risks and rewards incidental to ownership, are classified as finance leases. All other leases are classified as operating leases.

Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Lease payments are calculated using the interest rate implicit in the lease, or the Bank's incremental borrowing rate to identify the finance cost, which is recognised in profit or loss over the lease period, and the capital repayment, which reduces the liability to the lessor.

Payments made under operating leases, net of any incentives received from the lessor, are recognised in profit or loss on a straight-line basis over the term of the lease. Contingent rentals are expensed as they are incurred. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.11 Leases

(ii) Bank as lessor

Leases, where the Bank transfers substantially all the risks and rewards incidental to ownership, are classified as finance leases. All other leases are classified as operating leases.

Lease and instalment sale contracts are primarily financing transactions in banking activities, with rentals and instalments receivable, less unearned finance charges, being included in loans and advances in the statement of financial position.

Finance charges earned are computed using the effective interest method, which reflects a constant periodic rate of return on the investment in the finance lease. Initial direct costs and fees are capitalised to the value of the lease receivable and accounted for over the lease term as an adjustment to the effective rate of return. The tax benefits arising from investment allowances on assets leased to clients are accounted for in the direct taxation line.

Operating lease income from properties held as investment properties, net of any incentives given to lessees, is recognised on the straight-line basis or a more representative basis where applicable over the lease term. When an operating lease is terminated before the lease period has expired, any payment required by the bank by way of a penalty is recognised as income in the period in which termination takes place.

2.12 Provisions, contingent assets and contingent liabilities

Provisions are recognised when the bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Provisions are determined by discounting the expected future cash flows using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the liability.

The increase in provision due to passage of time is recognised as an expense.

Where there are a number of similar obligations, the probability that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Although the likelihood of outflow for any one item may be small, it may well be probable that some outflow of resources will be needed to settle the class of obligations as a whole.

A provision for restructuring is recognised when the Bank has approved a detailed formal plan, and the restructuring either has commenced or has been announced publicly. Future operating costs or losses are not provided for.

A provision for onerous contracts is recognised when the expected benefits to be derived by the bank from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the bank recognises any impairment loss on the assets associated with that contract.

Contingent assets are not recognised in the annual financial statements but are disclosed when, as a result of past events, it is probable that economic benefits will flow to the Bank, but this will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events which are not wholly within the Bank’s control.

Contingent liabilities include certain guarantees, other than financial guarantees, and letters of credit.

Contingent liabilities are not recognised in the annual financial statements but are disclosed in the notes to the annual financial statements unless they are remote.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.13 Taxation

(i) Direct tax

Current tax includes all domestic and foreign taxes based on taxable profits and capital gains tax. Current tax is determined for current period transactions and events and deferred tax is determined for future tax consequences. Current and deferred tax are recognised in profit or loss except to the extent that it relates to a business combination (relating to a measurement period adjustment where the carrying amount of the goodwill is greater than zero), or items recognised directly in equity or in OCI.

Current tax represents the expected tax payable on taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustments to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date.

Deferred tax is recognised for all taxable temporary differences, except:

- the initial recognition of goodwill;
- the initial recognition of assets and liabilities in a transaction that is not a business combination, which affects neither accounting nor taxable profits or losses, and
- investments in subsidiaries, associates and jointly controlled arrangements (excluding mutual funds) where the bank controls the timing of the reversal of temporary differences and it is probable that these differences will not reverse in the foreseeable future.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of the asset or liability and is not discounted.

Deferred tax assets are recognised to the extent that it is probable that future taxable income will be available against which the unused tax losses can be utilised. They 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.

Current and 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 income 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.

(ii) Indirect tax

Indirect taxes, including non-recoverable VAT, skills development levies and other duties for banking activities, are recognised in profit or loss and included in administrative expenses.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.14 Employee benefits

(i) Defined contribution plan

The Bank operates a number of defined contribution plans, based on a percentage of pensionable earnings funded by both employer companies and employees, the assets of which are generally held in separate trustee-administered funds.

Contributions to these plans are recognised as an expense in profit or loss in the periods during which services are rendered by employees.

The Bank and its employees also contribute to the National Social Security Fund, these contributions are determined by local statutes and the Bank's contributions are charged to profit or loss in the year which they relate to.

(ii) Termination benefits

Termination benefits are recognised as an expense when the Bank is committed, without realistic possibility of withdrawal, to a formal detailed plan to 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 as an expense if the Bank has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

(ii) Short-term benefits

Short-term benefits consist of salaries, accumulated leave payments, profit share, bonuses and any non-monetary benefits such as medical aid contributions.

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 plans or accumulated leave if the Bank 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.

2.15 Dividends

Dividends in ordinary shares are charged to equity in the period in which they are declared.

2.16 Equity

Ordinary shares are classified as 'share capital' in equity. Any premium received over and above the par value of the shares is classified as 'share premium' in equity.

(i) Share issue costs

Incremental external costs directly attributable to a transaction that increases or decreases equity are deducted from equity, net of related tax. All other share issue costs are expensed.

(ii) Distributions on ordinary shares

Distributions are recognised in equity in the period in which they are declared. Distributions declared after the reporting date is disclosed in the distributions note.

Proposed dividends are disclosed separately within equity until declared.

2.17 Earnings per share

Basic earnings per share are calculated by dividing the profit attributable to equity holders of the company by the weighted average number of ordinary shares in issue during the year. Diluted earnings per share is determined by adjusting the profit or loss attributable to ordinary share shareholders and the weighted average number of ordinary shared outstanding for the effects of all dilutive potential shareholders if any.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.18 Equity-linked transactions

Equity compensation plans

The Bank operates both equity-settled and cash-settled share-based compensation plans.

The fair value of equity-settled share options is determined on the grant date and accounted for as staff costs over the vesting period of the share options, with a corresponding increase in the share-based payment reserve. Non-market vesting conditions, such as the resignation of employees and retrenchment of staff, are not considered in the valuation but are included in the estimate of the number of options expected to vest. At each reporting date, the estimate of the number of options expected to vest is reassessed and adjusted against profit or loss and equity over the remaining vesting period.

On vesting of share options, amounts previously credited to the share-based payment reserve are transferred to retained earnings through an equity transfer. On exercise of equity-settled share options, proceeds received are credited to share capital and premium.

Share-based payments settled in cash are accounted for as liabilities at fair value until settled. The liability is recognised over the vesting period and is revalued at every reporting date and on settlement. Any changes in the liability are recognised in profit or loss.

2.19 Segment reporting

An operating segment is a component of the Bank engaged in business activities, whose operating results are reviewed regularly by management in order to make decisions about resources to be allocated to segments and assessing segment performance. The Bank's identification of segments and the measurement of segment results is based on the Bank's internal reporting to the excecutive committee.

Transactions between segments are priced at market-related rates.

2.20 Fiduciary activities

The bank commonly engages in trust or other fiduciary activities that result in the holding or placing of assets on behalf of individuals, trusts, post-employment benefit plans and other institutions. These assets and the income arising directly thereon are excluded from these annual financial statements as they are not assets of the bank. However, fee income earned and fee expenses incurred by the bank relating to the bank's responsibilities from fiduciary activities are recognised in profit or loss.

2.21 Hyperinflation

The South Sudan economy was classified as hyperinflationary from 1 January 2016. Accordingly, the results, cash flows and financial position of Stanbic South Sudan Branch have been expressed in terms of the measuring unit current at the reporting date. The results, cash flows and financial position have also been expressed in terms of the measuring unit current at the reporting date.

As the presentation currency of the Bank is that of a non-hyperinflationary economy, comparative amounts are not adjusted for changes in the price level or exchange rates in the current year. The prior period adjustments related to non-monetary items and differences arising on translation of comparative amounts are accounted for directly in retained earnings.

Non-monetary assets and liabilities are also restated at the date of initial application by applying to their cost and accumulated depreciation a general price index from the date the items were acquired to the date of initial application. The resulting adjustments determined at the beginning of the period are recognised directly in equity as an adjustment to opening retained earnings.

Notes (continued)

2 Summary of significant accounting policies (continued)

2.21 Hyperinflation (continued)

From the date of initial application and in subsequent periods, all components of owners' equity have been restated by applying a general price index from the beginning of the period or the date of contribution, if later. Items in the statement of financial position not already expressed in terms of the measuring unit current at the reporting period, such as non-monetary items carried at cost or cost less depreciation, are restated by applying a general price index. The restated cost, or cost less depreciation, of each item is determined by applying to its cost and accumulated depreciation the change in the general price index calculated from the later of the beginning of the reporting period and the date of acquisition up to the end of the reporting period. An impairment loss is recognised in profit or loss if the restated amount of a non-monetary item exceeds its estimated recoverable amount.

Restated retained earnings are derived from all other amounts in the restated statement of financial position.

All items recognised in the income statement are restated by applying the change in the general price index from the dates when the items of income and expenses were initially earned or incurred.

Gains or losses on the net monetary position are recognised in profit or loss within finance costs (Note 15).

2.22 Letters of Credit Acceptances

Letters of credit acceptances arise in two ways:

(i) Issuing Bank

At initial recognition where the Bank is the issuing bank. It recognises a contingent liability for the amount that it may be required to pay out to the confirming bank or beneficiary should the terms and conditions underlying the contract be met.

On the date that all terms and conditions underlying the contract are met, the Bank recognises a financial asset (at fair value) on the statement of financial position as part of loans and advances for the contractual right to receive cash from the applicant. Concurrently, the Bank recognises a financial liability (at fair value) on the statement of financial position as part of deposits for the contractual obligation to deliver cash to the beneficiary or the confirming bank, depending on the structure of the arrangement.

(ii) Confirming Bank

At initial recognition where the Bank is the confirming bank .It recognises the amount that it may be required to pay out to the beneficiary should the terms and conditions underlying the contract be met. The Bank concurrently recognises a contingent asset for the amount that the issuing bank may be entitled to receive.

On the date that all terms and conditions underlying the contract are met the Bank recognises a financial asset (at fair value) on the statement of financial position as part of loans and advances for the contractual right to receive cash from the issuing bank and concurrently recognises a financial liability (at fair value) on balance sheet as part of deposits for the contractual obligation to deliver cash to the beneficiary.

Notes (continued)

3 Critical accounting estimates and judgements in applying accounting policies

In preparing the financial statements, estimates and judgement are made that could materially affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on factors such as historical experience and current best estimates of uncertain future events that are believed to be reasonable under the circumstances.

Unless otherwise stated, no material changes to assumptions have occurred during the year.

3.1 Going concern

The Bank's management has made an assessment of its ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

3.2 Impairment of Fair value through OCI/ available–for–sale investment

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

3.3 Impairment of amortised cost/ held to maturity investment

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

3.4 Fair value of financial instruments

The fair value of financial instruments that are not quoted in active markets is determined using valuation techniques. Wherever possible, models use only observable market data. Where required, these models incorporate assumptions that are not supported by prices from observable current market transactions in the same instrument and are not based on available observable market data. Such assumptions include risk premiums, liquidity discount rates, credit risk, volatilities and correlations. Changes in these assumptions could affect the reported fair values of financial instruments.

The total amount of the change in fair value estimated using valuation techniques not based on observable market data that was recognised in profit or loss for the year ended 31 December 2018 was a profit of KShs nil (2017: KShs nil).

Additional disclosures on fair value measurements of financial instruments are set out in notes 2.6 and 5.

3.5 Development costs

The Bank capitalises software development costs for an intangible assets in accordance with the accounting policy detailed in note 2.8. Initial capitalisation of costs is based on management's judgment that technological and economic feasibility is confirmed, usually when a product development project has reached a defined milestone and where the Bank is able to demonstrate its intention and ability to complete and use the software.

3.6 Share-based payment

The Bank has a number of cash and equity-settled share incentive schemes which are issued to qualifying employees based on the rules of the schemes. The Bank uses the Black-Scholes option pricing model to determine the fair value of awards on grant date for its equity-settled share incentive schemes. The valuation of the Bank's obligation with respect to its cash-settled share incentive scheme obligations is determined with reference to the SBG share price, which is an observable market input. In determining the expense to be recognised for both the cash and equity-settled share schemes, the Bank estimates the expected future vesting of the awards by considering staff attrition levels. The Bank also makes estimates of the future vesting of awards that are subject to non-market vesting conditions by taking into account the probability of such conditions being met. Refer to note 41 for further details regarding the carrying amount of the liabilities arising from the Bank's cash-settled share incentive schemes and the expenses recognised in the income statement.

Notes (continued)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

3.7 Income taxes

The Bank is subject to direct taxation in two jurisdictions. There may be transactions and calculations for which the ultimate tax determination has an element of uncertainty during the ordinary course of business. The Bank recognises liabilities based on objective estimates of the quantum of taxes that may be due. Where the final tax determination is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions, disclosed in note 32 and note 33, respectively, in the period in which such determination is made.

Deferred tax assets

Deferred tax assets are recognised to the extent that it is probable that future taxable income will be available against which the unused tax losses 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.

Management's judgement surrounding the probability and sufficiency of future taxable profits, future reversals of existing taxable differences and on-going developments will determine the recognition of deferred tax. The most significant management assumption is the forecasts used to support the probability assessment that sufficient taxable profits will be generated by the entities in the bank in order to utilise the deferred tax assets.

Note 32 summarises the details of the carrying amount of the deferred tax assets. Accounting policy 2.13 provides further detail regarding the Bank's deferred tax accounting policy.

3.8 Hyperinflation

The Bank exercises significant judgement in determining the onset of hyperinflation in countries in which it operates and whether the functional currency of its branches is the currency of a hyperinflationary economy.

Various characteristics of the economic environment of each country are taken into account. These characteristics include, but are not limited to, whether:

- The general population prefers to keep its wealth in non-monetary assets or in a relatively stable foreign currency;
- Prices are quoted in a relatively stable foreign currency;
- Sales or purchase prices take expected losses of purchasing power during a short credit period into account;
- Interest rates, wages and prices are linked to a price index; and
- The cumulative inflation rate over three years is approaching, or exceeds, 100%.

Following management's assessment, the Bank's South Sudan branch has been accounted for as an entity operating in a hyperinflationary economy. The results, cash flows and financial position have been expressed in terms of the measuring units' current at the reporting date and the results and financial position.

The general price indices used in adjusting the results, cash flows and financial position of the branch is set out below:

The general price index used as published by the National Bureau of Statistics of South Sudan is as follows:

Date	Base year	General price index	Inflation rate
30 November 2018	2017	3,348.92	53.71%
30 September 2017	2016	2,178.73	78.68%

The impact of adjusting the Bank's results for the effects of hyperinflation is set out below:

Amount in Kshs'000	2018	2017
Net increase in revenue	**18,790**	553,439
Net monetary loss	**9,416**	255,266
Decrease in profit after tax	**(14,586)**	(179,974)

Notes (continued)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

3.9 Provisions

The accounting policy for provisions is set out in accounting policy 2.12 The principal assumptions taken into account in determining the value at which provisions are recorded at, in the bank's statement of financial position, include determining whether there is an obligation as well as assumptions about the probability of the outflow of resources and the estimate of the amount and timing for the settlement of the obligation.

The probability of an event of a significant nature occurring will be assessed by management and, where applicable, consultation with the Bank's legal counsel. In determining the amount and timing of the obligation once it has been assessed to exist, management exercises its judgement by taking into account all available information, including that arising after the statement of financial position date up to the date of the approval of the financial statements.

3.10 Expected credit loss (ECL) on financial assets - IFRS 9 drivers

ECL measurement period

Personal and business banking (PBB)

- The ECL measurement period at a minimum, is equal to the 12-month ECL of the financial asset.
- A loss allowance for full lifetime ECL is required for a financial asset if the credit risk of that financial instrument has increased significantly since initial recognition.
- The impact of the lifetime loss given default (LGD) workout, being an increase in the lifetime period over which subsequent cures and re-defaults are considered.
- The IFRS 9 requirement to hold ECL on unutilised loan commitments, notably pertaining to PBB's card and other lending portfolios.

Corporate and investment banking (CIB)

- The ECL measurement period at a minimum, is equal to the 12-month ECL of the financial asset.
- A loss allowance for full lifetime ECL is required for a financial asset if the credit risk of that financial instrument has increased significantly since initial recognition.
- The requirement to hold ECL on unutilised loan commitments has been included, where appropriate, within this classification.

Significant increase in credit risk (SICR) and low credit risk

A lifetime ECL requirement for all exposures for which there has been SICR. This included the impact of the LGD work out, being an increase in the life time period over which subsequent cures and re-defaults are considered. The requirement to hold ECL on off-balance sheet exposures has been included where appropriate within this classification.

PBB

In accordance with IFRS 9, all exposures are assessed to determine whether there has been SICR at the reporting date, in which case an impairment provision equivalent to the lifetime expected loss is recognised. SICR thresholds, which are behaviour score based, are derived for each portfolio vintage of exposures with similar credit risk and are calibrated over time to determine which exposures reflect deterioration relative to the originated population and consequently reflect an increase in credit risk.

The Bank also determines an appropriate transfer rate of exposures from stage 1 to stage 2 by taking into account the expected levels of arrears status for similar exposures. The SICR thresholds are reviewed regularly to ensure that they are appropriately calibrated to identify SICR throughout the life of the exposure and consequently facilitate appropriate

Where behaviour scores are not available, historical levels of delinquency are applied in determining whether there has been SICR. For all exposures, IFRS 9's non-rebuttable presumption of 30 days past due as well as exposures classified as either debt review or as 'watch-list' are used to classify exposures within stage 2.

Forward looking economic expectations are included in the ECL by adjusting the probability of default (PD), LGD and SICR. Adjustments are made based on the bank's macro-economic outlook, using models that correlate these parameters with macro-economic variables. Where modelled correlations are not viable or predictive, adjustments are based on expert judgement to predict the outcomes based on the bank's macro-economic outlook expectations.

Notes (continued)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

3.10 Expected credit loss (ECL) on financial assets - IFRS 9 drivers (continued)

ECL measurement period (continued)

CIB

The Bank uses a 25-point master rating scale to quantify the credit risk for each exposure. On origination, each client is assigned a credit risk grade within the bank's 25-point master rating scale. Ratings are mapped to PDs by means of calibration formulae that use historical default rates and other data for the applicable portfolio. These credit ratings are evaluated at least annually or more frequently as appropriate.

CIB exposures are evaluated for SICR by comparing the credit risk grade at the reporting date to the origination credit risk grade. Where the relative change in the credit risk grade exceeds certain pre-defined ratings' migration thresholds or, when a contractual payment becomes more than 30 days overdue (IFRS 9's rebuttable presumption), the exposure is classified within stage 2. These pre-defined ratings' migration thresholds have been determined based on historic default experience which indicate that higher rated risk exposures are more sensitive to SICR than lower risk exposures. Based on an analysis of historic default experience, exposures that are classified by the bank's master rating scale as investment grade are assessed for SICR at each reporting date but are considered to be of a low credit risk for IFRS 9 purposes.

Forward looking economic expectations are incorporated in CIB's client ratings. The client rating thus reflects the expected client risk for the bank's expectation of future economic and business conditions. Further adjustments, based on point-in-time market data, are made to the PDs assigned to each risk grade to produce PDs and ECL representative of existing market conditions.

Forward looking expectations

- The Bank Economics Research team determines the macroeconomic outlook and a Bank view of commodities over a planning horizon of at least three years. The outlook is provided to the legal entity Chief Financial Officer for review and asset and liability committee for approval.
- Macroeconomic outlooks take into account various variables such as gross domestic product, central bank policy interest rates, inflation, exchange rates and treasury bill rates.
- Narratives for each of the country economic outlooks, being bear, base and bull cases, are compiled and typically include consideration of the country's economic background, sovereign risk, foreign exchange risk, financial sector, liquidity and monetary policy stance.
- Probabilities are assigned to each of the bear, base and bull cases based on primary macroeconomic drivers and are reviewed monthly.
- The forward looking economic expectations are updated on a bi-annual basis or more regularly when deemed appropriate.

PBB

Adjustments to the PD and LGD, based on forward looking economic expectations at the reporting date resulted in the requirement to hold higher credit impairments.

CIB

Negligible impact as CIB's client ratings, used for IAS 39 purposes, typically included forward looking expectations.

Lifetime LGD work out

Increased lifetime period over which subsequent cures and re-defaults are considered resulted in higher credit impairments for credit-impaired financial assets.

Default

The Bank's definition of default has been aligned to its internal credit risk management definitions and approaches. Whilst the specific determination of default varies according to the nature of the product, it is generally determined (aligned to the Basel definition) as occurring at the earlier of:

- where, in the bank's view, the counterparty is considered to be unlikely to pay amounts due on the due date or shortly thereafter without recourse to actions such as the realisation of security; or
- when the counterparty is past due for more than 90 days (or, in the case of overdraft facilities in excess of the current limit).

Notes (continued)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

3.10 Expected credit loss (ECL) on financial assets - IFRS 9 drivers (continued)

Write off policy

An impaired loan is written off once all reasonable attempts at collection have been made and there is no economic benefit expected from attempting to recover the balance outstanding. The following criteria must be met before a financial asset can be written off:

- the financial asset has been in default for the period defined for the specific product (i.e. vehicle and asset finance, mortgage loans, etc.) which is deemed sufficient to determine whether the entity is able to receive any further economic benefit from the impaired loan; and
- at the point of write-off, the financial asset is fully impaired (i.e. 100% allowance) with the expectation that the probability of recovery is nil and this probability is not expected to change in the future.

As an exception to the above requirements, where the exposure is secured (or for collateralised structures), the impaired loan can only be written off once the collateral has been realised. Post-realisation of the collateral, the shortfall amount can be written off if it meets the second requirement listed above. The shortfall amount does not need to meet the first requirement to be written off.

Partial write-off of an asset occurs when the Bank gives a concession to a debtor such that a part of the loan will not be recovered. In this case, the part that will not be recovered is written off.

Curing

Continuous assessment is required to determine whether the conditions that led to a financial asset being considered to be credit impaired (i.e. stage 3) still exist. Financial assets that no longer qualify as credit impaired remain within stage 3 for a minimum period of six months (i.e. six full consecutive monthly payments per the terms and conditions). However, in the case of financial assets with quarterly or longer dated repayment terms, the classification of a financial asset out of stage 3 may be made subsequent to an evaluation by the Bank’s CIB or PBB Credit Governance Committee (as appropriate), such evaluation will take into account qualitative factors in addition to compliance with payment terms and conditions of the agreement. Qualitative factors include compliance with covenants and compliance with existing financial asset.

Where it has been determined that a financial asset no longer meets the criteria for significant increase in credit risk, when compared to the credit rating at initial recognition, the financial asset will be moved from stage 2 (lifetime expected credit loss model) back to stage 1 (12-month expected credit loss model) prospectively. In retail portfolios, a rehabilitation period of at least 6 months (subsequent to a customer repaying all outstanding facilities) would be needed for the customer’s internal rating to decrease back to its rating scale at initial recognition and move from stage 2 to stage 1 accordingly.

Debt financial investments

In terms of IFRS 9, this impairment provision is calculated per exposure for the shorter of 12 months or the remaining lifetime of the exposure. Such exposures generally did not carry an impairment provision in terms of IAS 39’s incurred loss impairment requirements.

Off-balance sheet exposures – bankers’ acceptances, guarantees and letters of credit

The requirement to hold ECL on off-balance sheet financial instruments, such as guarantees and letters of credit, resulted in a requirement to hold additional credit impairment provisions which were not held in terms of IAS 39.

Out of the above factors that drive the ECL, the most significant source of uncertainty is credit ratings allocated to counterparties which drive this assigned probability of default. The PDs in turn incorporate assessment for significant increase in credit risk, default risk assessment, forward looking information and probability weighted scenarios. At 31 December 2018, had the average credit ratings for all counterparties shifted one notch down expected credit losses would have increased by KShs 1,208,698,000 higher where if the credit ratings had shifted one notch up the excpected credit losses would have decreased by KShs 435,562,000.

Notes (continued)

3 Critical accounting estimates and judgements in applying accounting policies (continued)

3.11 Credit impairment lossses on loans and advances

(i) Portfolio loan impairments (IAS 39)

The Bank assesses its loan portfolios for impairment at each reporting date. In determining whether an impairment loss should be recorded in profit or loss, the Bank makes judgements as to whether there is observable data indicating a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be allocated to an individual loan in that portfolio.

Estimates are made of the duration between the occurrence of a loss event and the identification of a loss on an individual basis.

The impairment for performing and non-performing but not specifically impaired loans is calculated on a portfolio basis, based on historical loss ratios, adjusted for national and industry-specific economic conditions and other indicators present at the reporting date that correlate with defaults on the portfolio. These include early arrears and other indicators of potential default, such as changes in macroeconomic conditions and legislation affecting credit recovery. These annual loss ratios are applied to loan balances in the portfolio and scaled to the estimated loss emergence period.

	Average loss emergence period	
	2018*	**2017**
	Months	**Months**
Personal & Business Banking		
Mortgage loans	-	3
Instalment sale and finance leases	-	3
Card debtors	-	3
Other lending	-	3
Corporate & Investment Banking	**-**	**12**

** For 2018, refer to note 3.10*

(ii) Specific loan impairments

Non-performing loans include those loans for which the Bank has identified objective evidence of default, such as a breach of a material loan covenant or condition as well as those loans for which instalments are due and unpaid for 90 days or more. Management's estimates of future cash flows on individually impaired loans are based on historical loss experience for assets with similar credit risk characteristics.

The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. Where the net present value of estimated cash flows to differ by +/-1%, the impairment loss is to be estimated at KShs 76,988,000 higher or KShs 76,988,000 lower (2017: KShs 63,127,000 higher or KShs 63,127,000 lower).

Notes (continued)

4 Financial risk management

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

- Credit risk;
- Liquidity risk;
- Market risks; and
- Operational risks.

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

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

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

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

By their nature, the Bank's activities are principally related to the use of financial instruments including derivatives. The Bank accepts deposits from customers at both fixed and floating rates, and for various periods, and seeks to earn above-average interest margins by investing these funds in high quality assets. The Bank seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due. The Treasury identifies, evaluates and hedges financial risks in close co-operation with the Bank's operating units.

The Bank also seeks to raise its interest margins by obtaining above-average margins, net of allowances, through lending to commercial and retail borrowers with a range of credit standing. Such exposures involve not just on-statement of financial position loans and advances; the Bank also enters into guarantees and other commitments such as letters of credit and performance, and other bonds.

The Bank also trades in financial instruments where it takes positions in traded and over-the-counter instruments to take advantage of short-term market movements in bonds, currency and interest rate. The Board places trading limits on the level of exposure that can be taken in relation to both overnight and intra-day market positions.

Foreign exchange and interest rate exposures associated with derivatives are normally offset by entering into counter-balancing positions, thereby controlling the variability in the net cash amounts required to liquidate market positions.

Notes (continued)

4.1 Capital management

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of the statement of financial position, are:

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

It uses two approaches of measuring capital for capital management.

a) Economic capital assessment

Economic capital is the Bank's internal measure of required capital and it incorporates granular risk assessments and portfolio concentration effects that may be absent from the regulatory capital assessment process. Stanbic aggregates the individual risk type economic capital measurements conservatively assuming no inter-risk diversification. Economic capital is compared to Available Financial Reserves (AFR) to perform an assessment of capital adequacy based on internal measures.

b) Regulatory capital assessment

The Bank monitors the adequacy of its capital using ratios established by the Central Bank of Kenya (CBK), which ratios are broadly in line with those of the Bank for International Settlements (BIS).

These ratios measure capital adequacy by comparing the Bank's eligible capital with its statement of financial position assets, off-balance-sheet commitments and market and other risk positions at weighted amounts to reflect their relative risk.

The risk-based approach applies to both on and off-statement of financial position items. The focus of this approach is credit risk, interest rate risk, market risk, operational risk, concentration risk and underlying collateral risk.

The assets are weighted according to broad categories, each being assigned a risk weighting according to the amount of capital deemed to be necessary to support them. Four categories of risk weights (0%, 20%, 50%, and 100%) are applied.

The Bank is required at all times to maintain:

- A minimum level of regulatory capital of KShs 1 billion as at 31 December 2018;
- A core capital (tier 1) of not less than 10.5% (2017: 10.5%) of total risk weighted assets plus risk weighted off-statement of financial position items;
- A core capital (tier 1) of not less than 8% (2017: 8%)of its total deposit liabilities; and
- A total capital (tier 1 + tier 2) of not less than 14.5% (2017: 14.5%) of its total risk weighted assets plus risk adjusted off statement of financial position items.

Off-balance sheet credit related commitments and forwards are converted to credit risk equivalents using credit conversion factors, designed to convert these items into statement of financial position equivalents. The resulting credit equivalent amounts are then weighted for credit risk using the same percentages as for statement of financial position assets.

Notes (continued)

4 Financial risk management (continued)

4.1 Capital management (continued)

Tier 1 capital consists of shareholders' equity comprising paid up share capital, share premium and retained earnings less intangible assets, goodwill and investments in subsidiary institutions and equity instruments of other institutions. Tier 2 capital includes the Bank's term subordinated debt and regulatory loan loss reserves and cannot exceed tier 1 capital. Regulatory loan loss reserves qualifying as tier 2 capital cannot exceed 1.25% of the risk weighted assets total value.

The Bank has complied with these requirements. The Bank's capital adequacy level was as follows:

	2018 KShs'000	2017 KShs'000
Tier 1 capital (Core capital)		
Share capital	3,411,549	3,411,549
Share premium	3,444,639	3,444,639
Retained earnings	26,381,053	24,908,793
Total Tier 1 capital (Core capital)	**33,237,241**	**31,764,981**
Tier 2 capital		
Regulatory credit risk reserve	938,245	73
Qualifying subordinate liabilities	5,380,886	3,124,907
Total Tier 2 capital	**6,319,131**	**3,124,980**
Total capital (Tier 1 + Tier 2)	**39,556,372**	**34,889,961**
Risk - weighted assets		
Operational risk	33,099,577	31,767,770
Market risk	5,990,896	15,718,563
Credit risk on-statement of financial position	158,484,199	139,722,072
Credit risk off-statement of financial position	32,035,934	20,000,305
Total risk - weighted assets	**229,610,605**	**207,208,710**
Capital adequacy ratios		
Core capital / total deposit liabilities	16.5%	20.2%
Minimum statutory ratio	**10.5%**	**10.5%**
Core capital / total risk - weighted assets	14.6%	15.4%
Minimum statutory ratio	**10.5%**	**10.5%**
Total capital / total risk - weighted assets	17.4%	16.9%
Minimum statutory ratio	**14.5%**	**14.5%**

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk

Credit risk is the risk of loss arising out of failure of client counterparties to meet their financial or contractual obligations when due.

Credit risk is composed of counterparty risk (including primary, pre-settlement risk, issuer and settlement risk) and concentration risk. These risk types are defined as follows:

- Counterparty risk: The risk of credit loss to the Bank as a result of failure by a counterparty to meet its financial and/or contractual obligations to the Bank as they fall due.
- Credit concentration risk: The risk of loss to the Bank as a result of excessive build-up of exposure to a specific counterparty or counterparty group, an industry, market, product, financial instrument or type of security, or a maturity. This concentration typically exists where a number of counterparties are engaged in similar activities and have similar characteristics, which could result in their ability to meet contractual obligations being similarly affected by changes in economic or other conditions.

4.2.1 Governance committees

The primary governance committees overseeing credit risk are the Board Credit Committee (BCC) and Credit Risk Management Committee (CRMC). These committees are responsible for credit risk and credit concentration risk decision-making, and delegation thereof to Credit officers and committees within defined parameters.

Credit risk management is governed by the Bank's overall credit policy guidelines. Respective Credit Risk Management Divisions, which report into the BCC, are responsible for the implementation of these guidelines, which cover compliance with prescribed sanctioning authority levels, avoidance of a high concentration of credit risk and regular review of credit limits. Limits on facilities to counter-parties are governed by internal restraints, which restrict large exposures in relation to the Bank's capital.

The Bank has set in place comprehensive resources, expertise and controls to ensure efficient and effective management of credit risk.

4.2.2 General approach to managing credit risk

The Bank's credit risk comprises mainly wholesale and retail loans and advances, together with the counterparty credit risk arising from derivative contracts entered into with our clients and market counterparties.

The Bank manages credit risk through:

- maintaining strong culture of responsible lending and a robust risk policy and control framework;
- identifying, assessing and measuring credit risk clearly and accurately across the Bank , from the level of individual facilities up to the total portfolio;
- defining, implementing and continually re-evaluating our risk appetite under actual and scenario conditions;
- monitoring the Bank's credit risk relative to limits; and
- ensuring that there is expert scrutiny and independent approval of credit risks and their mitigation.

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.2 General approach to managing credit risk (continued)

Primary responsibility for credit risk management resides with the Bank's business lines. This is complemented with an independent credit risk function embedded within the business units, which is in turn supported by the overarching group risk function.

Impairment provisions are provided for losses that have been incurred at the statement of financial position date. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration of the Bank's portfolio, could result in losses that are different from those provided for at the reporting date. Management therefore carefully manages its exposure to credit risk.

The exposure to any one borrower including banks is further restricted by sub-limits covering on - and off-balance sheet exposures and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees, but a significant portion is personal lending where no such facilities can be obtained.

4.2.3 Management reporting

A number of reports are prepared as management information on credit risk. Various analysis of the data are done and a variety of reports are prepared on a monthly and quarterly basis. Some of these reports include:

- Monthly BCC Report;
- Quarterly Board Audit Report;
- Quarterly Board Risk Report;
- Regulatory returns;
- Half-year results; and
- Annual financial statements.

These reports are distributed to management, regulators and are available for inspection by authorised personnel.

4.2.4 Credit risk measurement

a) Loans and advances including loan commitments and guarantees

The estimation of credit exposure is complex and requires the use of models, as the value of a product varies with changes in market variables, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties.

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.4 Credit risk measurement (continued)

a) Loans and advances including loan commitments and guarantees (continued)

The Bank has developed models to support the quantification of the credit risk. These rating and scoring models are in use for all key credit portfolios and form the basis for measuring default risks. All models are managed under model development and validation policies that set out the requirements for model governance structures and processes, and the technical framework within which model performance and appropriateness is maintained. The models are developed using internal historical default and recovery data. In low default portfolios, internal data is supplemented with external benchmarks and studies. Models are assessed frequently to ensure on-going appropriateness as business environments and strategic objectives change, and are recalibrated annually using the most recent internal data.

In measuring credit risk of loans and advances to customers and to banks at a counter-party level, the Bank reflects three components:

(i) the ‘probability of default’ by the client or counter-party on its contractual obligations;

(ii) current exposures to the counter-party and its likely future development, from which the Bank derives the ‘exposure at default’; and

(iii) the likely recovery ratio on the defaulted obligations (the ‘loss given default’).

Probability of default (PD)

The Bank uses a 25-point master rating scale to quantify the credit risk for each borrower as illustrated in the table on the following page. Ratings are mapped to PDs by means of calibration formulae that use historical default rates and other data from the applicable portfolio. The bank distinguishes between through-the-cycle PDs and point-in-time PDs, and utilises both measures in decision-making and in managing credit risk exposures.

Loss given default (LGD)

Loss given default measures are a function of customer type, product type, seniority of loan, country of risk and level of collateralisation. LGDs are estimated based on historic recovery data per category of LGD. A downturn LGD is used in the estimation of the capital charge and reflects the anticipated recovery rates and macroeconomic factors in a downturn period.

Exposure at default (EAD)

Exposure at default captures the impact of potential draw-downs against unutilised facilities and changes in counterparty risk positions due to changes in market prices. By using historical data, it is possible to estimate the average utilisation of limits of an account when default occurs, recognising that customers may use more of their facilities as they approach default.

b) Debt securities

For debt securities, external rating such as Standard & Poor’s rating or their equivalents are used by Bank Treasury for managing of the credit risk exposures as supplemented by the Bank's own assessment through the use of internal ratings tools.

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.4 Credit risk measurement (continued)

Relationship between the bank master rating and external ratings

Core Banking system rating scale	Moody's Investor Services	Standard & Poor's	Fitch	Grading	Credit Quality
1 - 4	Aaa, Aa1, Aa2, Aa3	AAA, AA+, AA, AA-	AAA, AA+, AA, AA-	Investment grade	Normal monitoring
5 - 7	A1, A2, A3	A+, A, A-	A+, A, A-		
8 - 12	Baa1, Baa2, Baa3	BBB+, BBB, BBB-	BBB+, BBB, BBB-		
13 - 21	Ba1, Ba2, Ba3, B1, B2, B3	BB+, BB, BB-, B+, B, B-	BB+, BB, BB-, B+, B, B-	Sub-investment grade	
22 -25	Caa1, Caa2, Caa3, Ca	CCC+, CCC, CCC-	CCC+, CCC, CCC-		Close monitoring
Default	C	D	D	D	D

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.5 Risk limit control and mitigation policies

The Bank manages, limits and controls concentrations of credit risk wherever they are identified − in particular, to individual counterparties and banks, industries and countries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or banks of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, industry sector and country are approved quarterly by the Board of Directors.

The exposure to any one borrower including banks and brokers is further restricted by sublimit covering on-balance sheet and off-balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

Lending limits are reviewed in the light of changing market and economic conditions and periodic credit reviews and assessments of probability of default.

Some other specific control and mitigation measures are outlined below:

a) Credit tailored to customer profile

There is a clear distinction between the fundamental credit characteristics of the Bank's customer base. This customer base is managed according to the following market segments:

- Corporate and Investment Banking (CIB); and
- Personal and Business Banking (PBB)

The Bank has established separate credit management functions for each market segment.

Corporate and Investment Banking (CIB): Corporate, sovereign and bank portfolios

Corporate, sovereign and bank borrowers include Kenyan and international companies, sovereigns, local government entities, bank financial institutions, non-bank financial institutions and public sector entities. The entities include large companies as well as small and medium enterprises that are managed on a relationship basis. Creditworthiness is assessed based on a detailed individual assessment of the financial strength of the borrower. Exposure is usually in the form of short and long-term loans and advances but may include exposures arising from derivative contracts. In these sectors, credit risk management is characterised by a close working relationship between the counter-party, the customer relationship team and an independent credit evaluation manager. The credit evaluation manager bases his lending decision on an in-depth knowledge of the counterparty and the industry in which it operates, as well as an assessment of the creditworthiness of the counter-party based on a review of the audited financial statements and underlying risk parameters.

CIB believes that the use of sophisticated modelling techniques combined with an in-depth knowledge and understanding of each client is essential in properly assessing the credit risk, both initially and on an on-going basis, of each counterparty with whom it deals.

To this end CIB uses software developed by third party vendors, which is widely used by the banking industry globally in its credit management process. Expected default frequencies are an important tool in the formal credit assessment process of both new and existing business, and also form the basis for monitoring changes in counterparty credit quality on a day to day basis. Expected default frequencies will continue to be a vital component of credit risk management as the Bank continues to improve credit processes and increases focus on portfolio

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.5 Risk limit control and mitigation policies (continued)

a) Credit tailored to customer profile (continued)

Personal and Business Banking (PBB): Retail portfolio

Retail mortgage exposures relate to mortgage loans to individuals and are a combination of both drawn and undrawn EADs. Qualifying retail revolving exposure (QRRE) relate to cheque accounts, credit cards and evolving personal loans and products, and include both drawn and undrawn exposures. Retail other covers other branch lending and vehicle finance for retail, retail small and retail medium enterprise portfolios. Branch lending includes both drawn and undrawn exposures, while vehicle and asset finance only has drawn exposures.

Internally developed behavioural scorecards are used to measure the anticipated performance for each account. Mapping of the behaviour score to a PD is performed for each portfolio using a statistical calibration of portfolio-specific historical default experience. The behavioural scorecard PDs are used to determine the portfolio distribution on the master rating scale. Separate LGD models are used for each product portfolio and are based on historical recovery data. EAD is measured as a percentage of the credit facility limit and is based on historical averages. EAD is estimated per portfolio and per portfolio-specific segment, using internal historical data on limit utilisation

b) Financial covenants (for credit related commitments and loan books)

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

c) Master netting arrangements

The Bank further restricts its exposure to credit losses by entering into master netting arrangements with counterparties with which it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of assets and liabilities of the statement of financial position, as transactions are either usually settled on a gross basis or under most netting agreements the right of set off is triggered only on default. However, the credit risk associated with favourable contracts is reduced by a master netting arrangement to the extent that if a default occurs, all amounts with the counterparty are terminated and settled on a net basis. The Bank's overall exposure to credit risk on derivative instruments subject to master netting arrangements can change substantially within a short period, as it is affected by each transaction subject to the arrangement

d) Derivatives

For derivative transactions, the Bank typically uses internationally recognised and enforceable International Swaps and Derivatives Association (ISDA) agreements, with a credit support annexure, where collateral support is considered necessary. Other credit protection terms may be stipulated, such as limitations on the amount of unsecured credit exposure acceptable, collateralisation if mark-to-market credit exposure exceeds acceptable limits, and termination of the contract if certain credit events occur, for example, downgrade of the counterparty's public credit rating.

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.5 Risk limit control and mitigation policies (continued)

e) Collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The main types of collateral taken are:

Personal and Business Banking	
Mortgage lending	First ranking legal charge over the property financed.
Instalment sales	Joint registration of vehicles.
Other loans and advances	Debentures over the company's assets, cash cover in cash margin account, first ranking legal charge over both commercial and residential properties, directors' personal guarantees and company guarantees.

Corporate and Investment Banking	
Corporate lending	All assets debenture over the company's assets, cash cover in cash margin account, first ranking legal charge over both commercial and residential properties, directors' personal guarantees and company guarantees.

Longer-term finance and lending to corporate entities is generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimise possible credit loss the Bank seeks additional collateral from the counter-party as soon as impairment indicators are noticed for the relevant individual loans and advances.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured, with the exception of asset-backed securities and similar instruments, which are secured by portfolios of financial instruments.

Valuation of collateral

The Bank has a panel of valuers who undertake valuation of property and other assets to be used as Collateral. The valuers in the panel are qualified professional valuers with adequate experience in the field of property and machinery valuation. All the valuers on the panel provide the Bank with professional indemnity to cover the Bank in case of negligence. The Bank ensures that all properties used as collateral are adequately insured during the term of the loan. Valuation reports on properties are valid for three years after which the property and equipment is revalued.

The table on the following page shows the financial effect that collateral has on the Bank's maximum exposure to credit risk. The table includes collateral that management takes into consideration in the management of the bank's exposures to credit risk. All on- and off-balance sheet exposures that are exposed to credit risk, including non-performing loans, have been included. Collateral includes:

- Financial securities that have a tradable market, such as shares and other securities;
- Physical items, such as property, plant and equipment; and
- Financial guarantees and intangible assets.

Netting agreements, which do not qualify for offset under IFRS but which are nevertheless enforceable, are included as part of the bank's collateral for risk management purposes. All exposures are presented before the effect of any impairment provisions.

In the retail portfolio, 74% (2017: 92%) is fully collateralised. The total average collateral coverage for all retail mortgage exposures above 50% collateral coverage category is 100% (2017: 100%). Of the Bank's total exposure, 47% (2017: 51%) is unsecured and mainly reflects exposures to well-rated corporate counterparties, Bank counterparties and sovereign entities.

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.5 Risk limit control and mitigation policies (continued)

e) Collateral (continued)

31 December 2018	Total exposure	Unsecured exposure	Secured exposure	Netting agreements	Secured exposure after netting	Collateral coverage - Total: Greater than 0% to 50%	Greater than 50% to 100%	Greater than 100%
Asset class								
Corporate	**80,118,936**	14,170,709	65,948,227	-	**65,948,227**	-	65,948,227	-
Sovereign	**72,272,035**	72,272,035	-	-	**-**	-	-	-
Group	**21,306,058**	21,306,058	-	-	**-**	-	-	-
Retail	**77,735,641**	**9,937,393**	**67,798,248**	**-**	**57,637,510**	**-**	**57,637,510**	**-**
Retail mortgage	**21,013,697**	-	21,013,697	-	**21,013,697**	-	21,013,697	-
Other retail	**56,721,944**	9,937,393	46,784,551	-	**36,623,813**		36,623,813	-
Total	**251,432,670**	**117,686,195**	**133,746,475**	**-**	**123,585,737**	**-**	**123,585,737**	**-**
Less: Impairments for loans and advances	**(11,267,987)**							
Total exposure	**240,164,684**							

31 December 2017	Total exposure	Unsecured exposure	Secured exposure	Netting agreements	Secured exposure after netting	Collateral coverage - Total: Greater than 0% to 50%	Greater than 50% to 100%	Greater than 100%
Asset class								
Corporate	**112,912,959**	10,172,724	102,740,235	-	**102,740,235**	-	102,740,235	-
Sovereign	**81,938,218**	81,938,218	-	-	**-**	-	-	-
Group	**12,640,509**	12,640,509	-	-	**-**	-	-	-
Retail	**71,401,695**	**7,597,906**	**63,803,789**	**-**	**63,803,789**	**-**	**63,803,789**	**-**
Retail mortgage	**25,411,817**	-	25,411,817	-	**25,411,817**	-	25,411,817	-
Other retail	**45,989,878**	7,597,906	38,391,972	-	**38,391,972**	-	38,391,972	-
Total	**278,893,381**	**112,349,357**	**166,544,024**	**-**	**166,544,024**	**-**	**166,544,024**	**-**
Less: Impairments for loans and advances	**(5,264,005)**							
Total exposure	**273,629,376**							

The Bank holds collateral on loans and advances. The table below represents the collateral cover held on various types of loans and advances. Other deposits and margin balances held against off balance sheet facilities are included in other liabilities on note 36(a).

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.5 Risk limit control and mitigation policies (continued)

e) Collateral (continued)

Repossessed collateral

Assets repossessed as at the end of the year comprise saloon vehicles, prime movers and trailers, which had been financed by the Bank under Vehicle and Asset Finance (VAF) and residential and commercial property financed under personal markets. As at the year end, the Bank had taken possession of the following:

Nature of assets	2018 KShs' 000	2017 KShs' 000
Residential property	86,973	19,650
Other	294,908	265,976
	381,881	**285,626**

It is the Bank's policy to dispose of repossessed properties on the open market, at fair market value. The proceeds are used to reduce or repay the outstanding claim. In general, the Bank does not occupy repossessed properties for business use.

Renegotiated financial assets

Renegotiated loans and advances are exposures which have been refinanced, rescheduled, rolled over or otherwise modified following weaknesses in the counterparty's financial position, and where it has been judged that normal repayment will likely continue after the restructure. The renegotiations resulted in the continuation of the original financial asset, with no gain or loss recognised as a consequence of the restructuring. The table below show the carrying amount of financial assets whose term have been renegotiated, by class.

	2018 KShs' 000	2017 KShs' 000
Personal and Business Banking		
Instalment sales and finance leases	969,259	61,380
Other loans and advances	7,827,828	21,957
Corporate and Investment Banking		
Corporate lending	-	-
	8,797,087	**83,337**

4.2.6 Default and provisioning policy

The Bank's definition of default has been aligned to its internal credit risk management definitions and approaches. Whilst the specific determination of default varies according to the nature of the product, it is generally determined (aligned to the BASEL definition) as occurring at the earlier of:

- where, in the Bank's view, the counterparty is considered to be unlikely to pay amounts due on the due date or shortly thereafter; or
- when the counterparty is past due for more than 90 days (or, in the case of overdraft facilities in excess of the current limit).

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.6 Default and provisioning policy (continued)

The Bank does not rebut IFRS 9's 90 days past due rebuttable presumption.

A financial asset is considered to be in default when there is objective evidence of impairment. The following criteria are used in determining whether there is objective evidence of impairment for financial assets or groups of financial assets as per IFRS 9:

- significant financial difficulty of borrower and/or modification (i.e. known cash flow difficulties experienced by the borrower);
- a breach of contract, such as default or delinquency in interest and/or principal payments;
- disappearance of active market due to financial difficulties;
- it becomes probable that the borrower will enter bankruptcy or other financial reorganisation;
- where the Bank, for economic or legal reasons relating to the borrower's financial difficulty, grants the borrower a concession that the Bank would not otherwise consider.

Exposures which are overdue for more than 90 days are also considered to be in default.

Criteria for classification of loans and advances

IAS 39

The internal rating tool assists management to determine whether objective evidence of impairment exists under IAS 39, based on the following criteria set out by the Bank:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower (e.g. equity ratio, net income percentage of sales);
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral.

The credit quality of financial assets is managed by the Bank using the Bank's internal credit rating system. The credit rating system utilises both quantitative and qualitative information in arriving at the credit rating. Financial information is used and is key in arriving at the credit rating of individual borrowers. The qualitative information used in generating the credit rating includes quality of management, account operation and the industry in which the customer operates. The key consideration though remains the ability of the customer to meet its financial obligation from its cash flow.

Performing loans

Neither past due nor specifically impaired loans: are loans that are current and fully compliant with all contractual terms and conditions. Normal monitoring loans within this category are generally rated 1 to 21, and close monitoring loans are generally rated 22 to 25 using the Bank's master rating scale.

Early arrears but not specifically impaired loans: include those loans where the counterparty has failed to make contractual payments and payments are less than 90 days past due, but it is expected that the full carrying value will be recovered when considering future cash flows, including collateral. Ultimate loss is not expected but could occur if the adverse conditions persist.

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.6 Impairment and provisioning policy (continued)

Non-performing loans

Non-performing loans are those loans for which:

- the bank has identified objective evidence of default, such as a breach of a material loan covenant or condition; or

- instalments are due and unpaid for 90 days or more.

Non-performing specifically impaired loans: are those loans that are regarded as non-performing and for which there has been a measurable decrease in estimated future cash flows.

Specifically impaired loans are further analysed into the following categories:

- *Sub-standard:* Items that show underlying well-defined weaknesses and are considered to be specifically impaired.

- *Doubtful:* Items that are not yet considered final losses due to some pending factors that may strengthen the quality of the items.

- *Loss:* Items that are considered to be uncollectible in whole or in part. The bank provides fully for its anticipated loss, after taking collateral into account.

The impairment provision shown in the statement of financial position at 2017 year-end is derived from each of the five internal rating grades. However, the majority of the impairment provision comes from the bottom two grading (doubtful and loss categories).

4.2.7 Credit Quality

a) Maximum exposure to credit risk before collateral held or other credit enhancements

Financial instruments whose carrying amounts do not represent the maximum exposure to credit risk without taking account of any collateral held or other credit enhancements are disclosed in Note 22. The directors are confident in the ability to continue to control and sustain minimal exposure of credit risk to the Bank resulting from both the loan and advances portfolio and debt securities based on the following:

- 62% of the total maximum exposure is derived from loans and advances to customers (2017: 57%);28% represents investments in debt securities (2017: 22%);

- 76% of the loans and advances portfolio is categorised in the top two grades of the internal rating system (2017: 86%);

- 89% of the loans and advances portfolio are considered to be neither past due nor impaired (2017: 87%);

- 99% of all the debt securities, which the Bank has invested in, are issued by the Central Bank of Kenya (2017: 95%).

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.7 Credit Quality (continued)

b) Credit quality by class

The table below shows the credit quality by class of loans and advances, based on the Bank's credit rating system:

Year ended 31 December 2018	Gross Carrying amount	SB 1 - 12		SB 13 - 20		SB 21- 25		Default		Total gross carrying amount of default exposures	Securities and expected recoveries on default exposures	Interest in suspense on default exposures	Balance sheet expected credit loss on default exposures	Gross default coverage	Non-performing exposures
		Stage 1	Stage 2	Stage 1	Stage 2	Stage 1	Stage 2	Stage 3	Purchased/ originated credit impaired						
	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	%	%
Loans and advances to customers															
PBB	**76,393,937**	**-**	**-**	**51,536,603**	**-**	**-**	**20,073,035**	**4,784,299**	**-**	**4,784,299**	**1,560,942**	**638,133**	**2,585,224**	**59%**	**6%**
Mortgage loans	**21,024,031**	-	-	16,648,603	-	-	2,821,584	1,553,845	-	1,553,845	705,639	240,304	607,902	47%	7%
Vehicle and asset finance	**14,394,243**	-	-	9,829,299	-	-	3,328,484	1,236,459	-	1,236,459	202,880	129,533	904,046	76%	9%
Card debtors	**610,492**	-	-	-	-	-	610,492	-	-	-	(18,077)	-	18,077	100%	0%
Other loans and advances	**40,365,171**	-	-	25,058,701	-	-	13,312,475	1,993,995	-	1,993,995	670,500	268,296	1,055,199	59%	5%
CIB	**81,460,640**	**7,860,446**	**-**	**58,455,721**	**2,677,549**	**204,453**	**362,801**	**11,899,669**	**-**	**11,899,669**	**4,473,887**	**1,823,815**	**5,601,967**	**54%**	**15%**
Corporate	**81,460,640**	7,860,446	-	58,455,721	2,677,549	204,453	362,801	11,899,669	-	11,899,669	4,473,887	1,823,815	5,601,967	54%	15%
	157,854,577	**7,860,446**	**-**	**109,992,323**	**2,677,549**	**204,453**	**20,435,837**	**16,683,968**	**-**	**16,683,968**	**6,034,829**	**2,461,948**	**8,187,191**	**56%**	**11%**
Loans and advances to banks															
Bank	**28,295,159**	**27,556,215**	**-**	**738,944**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**583**	0%	0%
Gross carrying amount	**186,149,736**	**35,416,661**	**-**	**110,731,267**	**2,677,549**	**204,453**	**20,435,837**	**16,683,968**	**-**	**16,683,968**	**6,034,829**	**2,461,948**	**8,187,774**	**56%**	**9%**
Less: Total expected credit losses for loans and advances	**(11,251,043)**														
Net carrying amount of loans & advances measured at amortised cost	**174,898,693**														

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.7 Credit Quality (continued)

b) Credit quality by class (continued)

	Gross Carrying amount KShs'000	SB 1 - 12		SB 13 - 20		SB 21- 25		Default	
		Stage 1 KShs'000	Stage 2 KShs'000	Stage 1 KShs'000	Stage 2 KShs'000	Stage 1 KShs'000	Stage 2 KShs'000	Stage 3 KShs'000	Purchased/originated credit impaired KShs'000
Financial investments measured at amortised									
Corporate	**708,676**	662,092	-	-	46,585	-	-	-	-
Sovereign	**22,509,806**	17,386,449	-	5,123,357	-	-	-	-	-
Bank	**-**	-	-	-	-	-	-	-	-
Mutual funds and unit-linked investments	**-**	-	-	-	-	-	-	-	-
Other instruments	**-**	-	-	-	-	-	-	-	-
Gross carrying amount	**23,218,483**								
Less: Total expected credit losses for financial investments at amortised cost	**(17,527)**								

	Gross Carrying amount KShs'000	SB 1 - 12 Stage 1 KShs'000	SB 1 - 12 Stage 2 KShs'000	SB 13 - 20 Stage 1 KShs'000	SB 13 - 20 Stage 2 KShs'000	SB 21- 25 Stage 1 KShs'000	SB 21- 25 Stage 2 KShs'000	Default Stage 3 KShs'000	Default Purchased/originated credit impaired KShs'000
Financial investments at fair value through OCI									
Corporate	**-**	-	-	-	-	-	-	-	-
Sovereign	**17,853,280**	17,853,280	-	-	-	-	-	-	-
Bank	**-**	-	-	-	-	-	-	-	-
Mutual funds and unit-linked investments	**-**	-	-	-	-	-	-	-	-
Other instruments	**-**	-	-	-	-	-	-	-	-
Gross carrying amount	**17,853,280**								
Add: Fair value reserve ralating to fair value adjustments (before the ECL balance)	**(1,763)**								

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.7 Credit Quality (continued)

b) Credit quality by class (continued)

The table below shows the credit quality by class of loans and advances, based on the Bank's credit rating system:

Year ended 31 December 2017			Performing loans				Non-performing loans (NPL)										
			Neither past due nor specifically impaired		Past due but not specifically impaired		Specifically impaired loans										
							NPL NET OF IIS (interest in suspense)										
	Total loans and advances KShs'000 2017	Balance sheet impairments for performing loans KShs'000 2017	Normal monitoring KShs'000 2017	Close monitoring KShs'000 2017	Early arrears KShs'000 2017	Non-performing KShs'000 2017	Sub-standard KShs'000 2017	Doubtful KShs'000 2017	Loss KShs'000 2017	Total KShs'000 2017	Securities and expected recoveries on specifically impaired loans KShs'000 2017	Net after securities and expected recoveries on specifically impaired loans KShs'000 2017	Balance sheet impairments for non-performing specifically impaired loans KShs'000 2017	Gross specific impairment coverage %	Total non-performing loans KShs'000 2017	Non-performing loans %	Interest in Suspense KShs'000 2017
	N=A=B=C+L		A	B	C	D	E	F	G	H=E+F+G	I	J=H-I	K		L=H+D		M
Personal and Business Banking	**65 639 943**	**378 864**	**48 122 211**	**7 168 528**	**6 832 168**	**-**	**1 171 006**	**2 077 483**	**268 548**	**3 517 037**	**1 884 756**	**1 632 281**	**1 632 281**	**46%**	**3 517 037**	**5%**	**503 268**
- Mortgage lending	**25 411 817**	**122 694**	**18 964 809**	**2 818 329**	2 714 021	-	155 217	757 502	1 938	**914 658**	663 910	250 748	250 748	**27%**	914 658	**4%**	208 988
- Instalment sales and finance leases	13 149 039	89 734	9 064 565	356 683	2 408 572	-	422 076	873 041	24 102	**1 319 219**	591 806	727 413	727 413	**55%**	1 319 219	**10%**	149 453
- Card debtors	575 242	7 733	504 102	-	48 033	-	-	-	23 108	**23 108**	4 901	18 207	18 206	**79%**	23 108	**4%**	-
- Other loans and advances	26 503 845	158 703	19 588 735	3 993 516	1 661 542	-	593 713	446 940	219 400	**1 260 053**	624 139	635 914	635 914	**50%**	**1 260 053**	**5%**	144 827
Corporate and Investment Banking	**70 159 872**	**1 641 540**	**56 186 734**	**4 408 933**	**4 353 318**	**-**	**-**	**5 182 008**	**28 879**	**5 210 887**	**3 599 567**	**1 611 320**	**1 611 320**	**31%**	**5 210 887**	**7%**	**1 160 705**
- Corporate lending	**70 159 872**	1 641 540	56 186 734	4 408 933	4 353 318			5 182 008	28 879	**5 210 887**	3 599 567	**1 611 320**	1 611 320	**31%**	5 210 887	**7%**	1 160 705
															-		
Gross loans and advances to customers	**135 799 815**	**2 020 404**	**104 308 945**	**11 577 461**	**11 185 486**	**-**	**1 171 006**	**7 259 491**	**297 427**	**8 727 924**	**5 484 323**	**3 243 601**	**3 243 601**	**37%**	**8 727 924**	**6%**	**1 663 973**
Percentage of total book (%)	100.0%	1.5%	76.8%	8.5%	8.2%	0.0%	0.9%	5.3%	0.2%	6.4%	4.0%	2.4%	2.4%		6.4%		1.2%
Less:																	
Impairment for performing Loans and advances	(2 020 404)																
Impairment for non performing Loans and advances	(3 243 601)																
Net loans and advances	**130 535 810**																

Notes (continued)

4 Financial risk management (continued)

4.2 Credit risk (continued)

4.2.7 Credit Quality (continued)

c) Ageing analysis of past due but not impaired financial assets

Loans and advances less than 90 days past due are not considered impaired unless other information is available to indicate the contrary.

The table below shows the ageing of financial assets that are past due at the reporting date but not impaired, per class.

	Performing (Early arrears)			Non - performing		Total
	1 to 29 days	30 to 59 days	60 to 89 days	90 to 180 days	More than 180 days	
31 December 2018	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Personal and Business Banking	**13,459,417**	**3,148,911**	**1,818,619**	**-**	**-**	**18,426,947**
Mortgage lending	2,177,993	757,608	376,744	-	-	***3,312,345***
Instalment sales and finance leases	2,101,589	785,140	168,876	-	-	***3,055,605***
Other loans and advances	9,179,835	1,606,163	1,272,999	-	-	***12,058,997***
Corporate and Investment Banking	**13,603,508**	**126,475**	**341,260**	**-**	**-**	**14,071,244**
Corporate lending	13,603,508	126,475	341,260	-	-	**14,071,244**
Total recognised financial instruments	**27,062,925**	**3,275,386**	**2,159,879**	**-**	**-**	**32,498,191**
31 December 2017						
Personal and Business Banking	**4,733,200**	**1,482,944**	**616,024**	**-**	**-**	**6,832,168**
Mortgage lending	1,745,427	705,774	262,821	-	-	**2,714,022**
Instalment sales and finance leases	1,756,159	508,797	143,616	-	-	**2,408,572**
Other loans and advances	1,231,614	268,373	209,587	-	-	**1,709,574**
Corporate and Investment Banking	**3,328,461**	**539,013**	**485,844**	**-**	**-**	**4,353,318**
Corporate lending	3,328,461	539,013	485,844	-	-	***4,353,318***
Total recognised financial instruments	**8,061,661**	**2,021,957**	**1,101,868**	**-**	**-**	**11,185,486**

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk

Market risk is the risk of a change in market value, earnings (actual or effective) or future cash-flows of a portfolio of financial instruments (including commodities), caused by moves in market variables such as equity, bond and commodity prices, currency exchange rates and interest rates, credit spreads, recovery rates, correlations and implied volatilities in all of these measures.

4.3.1 Governance committees

The Bank's policy is that all trading activities are undertaken within the Bank's trading operations. The Board grants general authority to take on market risk exposure to the Bank's Assets and Liabilities Committee (ALCO).

Market risk management process is required to measure, monitor and control market risk exposures. The Bank manages market risk through following four principles.

i) Identification of market risks in the trading and banking books

This process entails checking that all market risks are identified. It includes an analysis of new business plans, new products, new pricing models, new risk models and regular reviews by Market Risk staff of financial and management accounts balance sheets, income statements, and portfolio structure hierarchies, accounting classification and accounting elections, jointly with financial control, Risk Self Assessments jointly with operational risk, price testing reports and profit and loss decomposition reports.

ii) Measurement of market risk

Measurement of market risks deals specifically and separately with normal market conditions and stress market conditions. Measurement of trading exposures under stress market conditions is effected by subjecting the portfolios to stress testing, e.g. historical scenarios, hypothetical scenarios on individual asset classes and across different asset classes. In order to highlight 'points of weakness' and identify particular sources of trading book exposure vulnerability, these stress tests capture the effects of abnormal movements in market variables (yield curves including basis curves, volatility surfaces, spot and/or rate moves, credit spread curves, recovery rate sensitivities etc.).

iii) Management of market risk

The Bank manages market risk through a specification of risk appetite in form of market risk limits. It uses a suite of risk measurement techniques, including Value at Risk (VaR), Stress Value at Risk (SVar), stress testing, stop loss triggers, back-testing and specific business unit and product controls.

iv) Reporting of market risk

Market Risk has reporting procedures that highlight for attention within Market Risk or by management all forms of exposures i.e. limit breaches or other reports that will periodically be required to submit to different stakeholders e.g. Local ALCO, Local Board, Internal Capital Adequacy Assessment Process (ICAAP) stakeholders, Shareholders (Annual financial statements); Rating agencies; Central Bank of Kenya and other regulators.

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.2 Market risk exposure on banking operations

Banking-related market risk exposure principally involves the management of the potential adverse effect of interest rate movements on net interest income and the economic value of equity that arise from structural interest rate risk caused by the differing repricing characteristics of banking assets and liabilities. They include endowment risk, repricing risk, basis risk, optionality risk and yield curve risk. The Bank's approach to managing Interest Rate Risk in Banking Book (IRRBB) is governed by applicable regulations and is influenced by the competitive environment in which the Bank operates. Treasury and Capital Management team monitors banking book interest rate risk together with the country ALCO.

The market risk function is independent of trading operations and it is accountable to ALCO. It is responsible for identifying, measuring, managing, controlling and reporting market risk as outlined in the market risk governance standard, with support from the central market risk function. The market risk function also has the ability to set individual trader mandates. Exposures and excesses are monitored and reported daily. Where breaches in limits and triggers occur, actions are taken by market risk management unit to move exposures back in line with approved market risk appetite, with such breaches being reported to management and ALCO.

4.3.3 Approved regulatory capital approaches

The Bank applies the Standardised approach for calculating market risk capital. The standardised method uses a “building block” approach, with the capital charge for each risk category calculated separately.

Market risk qualifying assets includes interest rate risk assets in the trading book and foreign currency risk assets throughout the Bank.

4.3.4 Trading book market risk

Trading book market risk is represented by financial instruments held on the trading book, arising out of normal global markets' trading activity.

4.3.5 Approach to managing market risk in the trading book

The Stanbic Bank policy is that all trading activities are undertaken within the Bank's trading operations. The market risk functions are independent of trading operations and accountable to ALCO. All Value at Risk (VaR) and stressed VaR (SVaR) limits require prior approval from ALCO. The market risk functions have the authority to set limits at a lower level.

Market risk teams are responsible for identifying, measuring, managing, monitoring and reporting market risk as outlined in the market risk governance standard.

Exposures and excesses are monitored and reported daily. Where breaches in limits and triggers occur, actions are taken by market risk functions to move exposures back in line with approved market risk appetite, with such breaches being reported to management and ALCO.

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.5 Approach to managing market risk in the trading book (continued)

a) VaR and SVaR

The Bank uses the historical VaR and SVaR approach to quantify market risk under normal conditions and under stressed conditions.

For risk management purposes VaR is based on 250 days of unweighted recent historical data, a holding period of one day and a confidence level of 95%. The historical VaR results are calculated in four steps:

- Calculate 250 daily market price movements based on 250 days' historical data.
- Calculate hypothetical daily profit or loss for each day using these daily market price movements.
- Aggregate all hypothetical profits or losses for day one across all positions, giving daily hypothetical profit or loss, and then repeat for all other days.
- VaR is the 95th percentile selected from the 250 days of daily hypothetical total profit or loss.

Daily losses exceeding the VaR are likely to occur, on average, 13 times in every 250 days.

SVaR uses a similar methodology to VaR, but is based on a period of financial stress and assumes a 10-day holding period and a 99% confidence interval.

Where the Bank has received internal model approval, the market risk regulatory capital requirement is based on VaR and SVaR, both of which use a confidence level of 99% and a 10-day holding period.

Limitations of historical VaR are acknowledged globally and include:

- The use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature.
- The use of a one-day holding period assumes that all positions can be liquidated or the risk offset in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully.
- The use of a 95% confidence level, by definition, does not take into account losses that might occur beyond this level of confidence.
- VaR is calculated on the basis of exposures outstanding at the close of business and, therefore, does not necessarily reflect intraday exposures.
- VaR is unlikely to reflect loss potential on exposures that only arise under significant market moves.

b) Stop-loss triggers

Stop-loss triggers are used to protect the profitability of the trading desks, and are monitored by market risk on a daily basis. The triggers constrain cumulative or daily trading losses through acting as a prompt to a review or close-out positions.

c) Stress tests

Stress testing provides an indication of the potential losses that could occur under extreme but plausible market conditions, including where longer holding periods may be required to exit positions. Stress tests comprise individual market risk factor testing, combinations of market factors per trading desk and combinations of trading desks using a range of historical and hypothetical simulations. Daily losses experienced during the year ended 31 December 2018 did not exceed the maximum tolerable losses as represented by the Bank's stress scenario limits.

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.5 Approach to managing market risk in the trading book (continued)

d) Back-testing

The Bank back-tests its VaR models to verify the predictive ability of the VaR calculations and ensure the appropriateness of the models within the inherent limitations of VaR. Back-testing compares the daily hypothetical profit and losses under the one-day buy and hold assumption to the prior day's calculated VaR In addition, VaR is tested by changing various model parameters, such as confidence intervals and observation periods to test the effectiveness of hedges and risk-mitigation instruments.

e) Specific business unit and product controls

Other market risk limits and controls specific to individual business units include permissible instruments, concentration of exposures, gap limits, maximum tenor, stop-loss triggers, price validation and balance sheet substantiation.

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.6 Foreign exchange risk

Definition

The Bank's primary exposures to foreign currency risk arise as a result of the translation effect on the bank's net assets in foreign operations, intragroup foreign-denominated debt and foreign denominated cash exposures and accruals.

Approach to managing foreign currency risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Asset and Liability Committee sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily risk according to existing legislation, and accounting parameters. It takes into account naturally offsetting risk positions and manages the bank's residual risk by means of forward exchange contracts, currency swaps and option contracts.

Hedging is undertaken in such a way that it does not constrain normal operational activities. In particular, the need for capital to fluctuate with risk-weighted assets is taken into account.

The repositioning of the currency profile is a controlled process based on underlying economic views of the relative strength of currencies. The Bank does not ordinarily hold open exposures of any significance with respect to the banking book.

Gains or losses on derivatives are reported in profit or loss.

The table below summarises the Bank's exposure to foreign exchange risk at 31 December 2018.

Included in the table are the Bank's financial instruments at carrying amounts, categorised by currency (all amounts expressed in millions of Kenya Shillings):

At 31 December 2018	USD	GBP	EUR	Others	Total
Assets					
Cash and bank balances with banks abroad	18,930	851	1,003	1,639	**22,423**
Loans and advances	62,795	740	3,266	13	**66,815**
Investment in government securities	5,177	-	-	664	**5,842**
Balances due from group companies	20,048	3	-	950	**21,001**
Other foreign currency assets	2,326	0	295	588	**3,210**
Total foreign denominated financial assets	**109,277**	**1,594**	**4,565**	**3,855**	**119,291**
Liabilities					
Amounts due to banking institutions abroad	23,476	10	531	707	**24,723**
Deposits	70,116	9,422	5,865	1,446	**86,848**
Loans and advances	3,344	-	-	-	**3,344**
Balances due to group companies	13,157	-	220	-	**13,377**
Other foreign currency liabilities	4,534	3	3,596	1,126	**9,258**
Total foreign denominated financial liabilities	**114,626**	**9,434**	**10,212**	**3,279**	**137,551**
Net on balance sheet financial position	(5,349)	(7,840)	(5,646)	575	**(18,260)**
Off balance sheet net notional position	6,351	7,858	5,862	1,073	**21,144**
Overall net position	**1,003**	**18**	**216**	**1,648**	**2,884**

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.6 Foreign exchange risk (continued)

At 31 December 2017	USD	GBP	Euro	Others	Total
Assets					
Cash and bank balances with banks abroad	14,703	427	661	2,780	**18,571**
Loans and advances	59,601	391	5,649	1	**65,642**
Investment in Government Securities	2,141	-	-	1	**2,142**
Balances due from Group Companies	2,581	-	-	210	**2,791**
Other foreign currency assets	2,851	22	397	974	**4,244**
Total foreign denominated financial assets	**81,877**	**840**	**6,707**	**3,966**	**93,390**
Liabilities					
Amounts due to banking institutions abroad	29,782	8	186	616	**30,592**
Deposits	55,221	1,851	6,327	1,684	**65,083**
Loans and advances	-	-	-	-	**-**
Balances due to Group Companies	9,911	-	1,637	-	**11,548**
Other foreign currency liabilities	5,182	8	137	1,260	**6,587**
Total foreign denominated financial liabilities	**100,096**	**1,867**	**8,287**	**3,560**	**113,810**
Net on balance sheet financial position	(18,219)	(1,027)	(1,580)	406	**(20,420)**
Off balance sheet net notional position	20,414	1,036	2,098	(720)	**22,828**
Overall net position	**2,195**	**9**	**518**	**(314)**	**2,408**

The table below indicates the extent to which the Bank was exposed to currency risk as at 31 December on its monetary assets and liabilities denominated in foreign currency. The table shows the sensitivity analysis for each currency to which the Bank has significant exposure and the effect of the change in exchange rate on income statement.

Year ended 31 December 2018 Currency	Increase in currency rate in % 2018	Effect on profit before tax 2018 KShs'000	Effect on equity 2018 KShs'000	Decrease in currency rate in % 2018	Effect on profit before tax 2018 KShs'000	Effect on equity 2018 KShs'000
USD	**0.92%**	9,225	6,457	**1.09%**	10,929	7,650
GBP	**2.70%**	606	424	**2.34%**	525	367
EUR	**2.19%**	5,407	3,785	**2.01%**	4,963	3,474

Year ended 31 December 2017 Currency	Increase in currency rate in % 2017	Effect on profit before tax 2017 KShs'000	Effect on equity 2017 KShs'000	Decrease in currency rate in % 2017	Effect on profit before tax 2017 KShs'000	Effect on equity 2017 KShs'000
USD	**0.82%**	17,991	12,593	**0.79%**	17,333	12,133
GBP	**2.92%**	325	228	**2.91%**	324	227
EUR	**1.93%**	11,989	8,392	**2.62%**	16,275	11,393

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.7 Interest rate risk

Interest rate risk in the banking book (IRRBB)

These are risks that have an impact on net interest income that arise from structural interest rate risk caused by the differing repricing characteristics of banking assets and liabilities.

IRRBB is further divided into the following sub risk types:

- **Repricing risk:** timing differences in the maturity (fixed rate) and repricing (floating rate) of assets and liabilities.
- **Yield curve risk:** shifts in the yield curves that have adverse effects on the Bank's income or underlying economic value.
- **Basis risk:** hedge price not moving in line with the price of the hedged position. Examples include bonds/swap basis, futures/ underlying basis.
- **Optionality risk:** options embedded in bank asset and liability portfolios, providing the holder with the right, but not the obligation, to buy, sell, or in some manner alter the cash flow of an instrument or financial contract.
- **Endowment risk:** exposure arising from the net differential between interest rate insensitive assets such as non-earning assets, interest rate insensitive liabilities such as non-paying liabilities, and equity.

Approach to managing IRRBB

Banking book-related market risk exposure principally involves managing the potential adverse effect of interest rate movements on banking book earnings (net interest income and banking book mark-to-market profit or loss) and the economic value of equity.

The Bank's approach to managing IRRBB is governed by applicable regulations and is influenced by the competitive environment in which the Bank operates. The Bank's Treasury and Capital Management team monitors banking book interest rate risk operating under the oversight of ALCO.

Measurement

The analytical techniques used to quantify IRRBB include both earnings- and valuation-based measures. The analysis takes account of embedded optionality such as loan prepayments and accounts where the account behaviour differs from the contractual position.

The results obtained from forward-looking dynamic scenario analyses, as well as Monte Carlo simulations, assist in developing optimal hedging strategies on a risk-adjusted return basis.

Desired changes to a particular interest rate risk profile are achieved through the restructuring of on-balance sheet repricing or maturity profiles, or through derivative overlays.

Limits

Interest rate risk limits are set in relation to changes in forecast banking book earnings and the economic value of equity. Economic value of equity sensitivity is calculated as the net present value of aggregate asset cash flows less the net present value of aggregate liability cash flows.

All assets, liabilities and derivative instruments are allocated to gap intervals based on either their repricing or maturity characteristics. Assets and liabilities for which no identifiable contractual repricing or maturity dates exist are allocated to gap intervals based on behavioural profiling.

Notes (continued)

4 Financial risk management (continued)

4.3 Market risk (continued)

4.3.7 Interest rate risk (continued)

Hedging of endowment risk

IRRBB is predominantly the consequence of endowment exposures, being the net effect of non-rate sensitive assets less non-rate sensitive liabilities and equity.

The endowment risk is hedged using liquid instruments as and when it is considered opportune. Where permissible, hedge accounting is adopted using the derivatives. The interest rate view is formulated through ALCO processes, following meetings of the monetary policy committees, or notable market developments.

Non-endowment IRRBB (repricing, yield curve, basis and optionality) is managed within the treasury and the global markets portfolios.

The table below indicates the KShs equivalent sensitivity of the Bank's banking book earnings (net interest income and banking book mark-to-market profit or loss) and other comprehensive income (OCI) given a parallel yield curve shock. A floor of 0% is applied to all interest rates under the decreasing interest rate scenario. Hedging transactions are taken into account while other variables are kept constant.

	Increase in basis points	Sensitivity of net interest income	Sensitivity of other comprehensive income	Decrease in basis points	Sensitivity of net interest income	Sensitivity of other comprehensive income
	2018	2018	2018	2018	2018	2018
Currency	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
KShs	250	815,205	(22,084)	200	(542,511)	17,668
Others*	100	3,250	-	100	(33,954)	-

	Increase in basis points	Sensitivity of net interest income	Sensitivity of other comprehensive income	Decrease in basis points	Sensitivity of net interest income	Sensitivity of other comprehensive income
	2017	2017	2017	2017	2017	2017
Currency	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
KShs	350	948,553	(1,153,661)	300	(1,345,202)	988,852
Others*	100	3,735	-	100	(2,751)	-

** These are any other currencies held by the Bank not denominated in KShs.*

Notes (continued)
4 Financial risk management (continued)

4.4 Liquidity risk

Liquidity risk arises when the Bank, despite being solvent, is unable to maintain or generate sufficient cash resources to meet its payment obligations as they fall due, or can only do so on materially disadvantageous terms. This inability to maintain or generate sufficient cash resources may arise where counterparties who provide the Bank with short-term funding withdraw or do not rollover that funding, or normally liquid assets become illiquid as a result of a generalised disruption in asset markets.

The nature of banking and trading activities results in a continuous exposure to liquidity risk. The Bank manages liquidity in accordance with applicable regulations and within Bank's risk appetite. The Bank's liquidity risk management governance framework supports the measurement and management of liquidity at various levels to ensure that all payment obligations can be met by the Bank under both normal and stressed conditions. Liquidity risk management ensures that the Bank has the appropriate amount, diversification and tenor of funding and liquidity to support its asset base at all times.

The Bank's liquidity risk management framework differentiates between:

- **Tactical (shorter-term) risk management:** managing intra-day liquidity positions and daily cash flow requirements, and monitoring adherence to prudential and internal requirements and setting deposit rates as informed by ALCO.

- **Structural (long-term) liquidity risk management:** ensuring a structurally sound statement of financial position, a diversified funding base and prudent term funding requirements.

- **Contingent liquidity risk management:** monitoring and managing early warning liquidity indicators while establishing and maintaining contingency funding plans, undertaking regular liquidity stress testing and scenario analysis, and setting liquidity buffers in accordance with anticipated stress events.

Governance committees

The primary governance committee overseeing this risk is the Bank Asset Liability Committee (ALCO), which is chaired by the Chief Executive. There is independent risk oversight of all liquidity limits and guidelines by Market Risk, Finance and Central Asset Liability Management units. ALCO reports to the Board Risk Committee.

Approach to managing liquidity risk

There is a sound and robust liquidity management process to measure, monitor and manage liquidity exposures. The following elements are incorporated as part of a cohesive liquidity management process:

a) *Maintaining a structurally sound statement of financial position;*
With actual cash flows typically varying significantly from the contractual position, behavioural profiling is applied to assets, liabilities and off-balance sheet commitments with an indeterminable maturity or drawdown period, as well as to certain liquid assets. Behavioural profiling assigns probable maturities based on historical customer behaviour. This is used to identify significant additional sources of structural liquidity in the form of liquid assets and core deposits, such as current and savings accounts, which exhibit stable behaviour despite being repayable on demand or at short notice.

Structural liquidity mismatch analysis are performed regularly to anticipate the mismatch between payment profiles of balance sheet items, in order to highlight potential risks within the Bank's defined liquidity risk thresholds.

b) *Foreign currency liquidity management;*
A specific number of indicators are observed in order to monitor changes in market liquidity as well as the impacts on liquidity as a result of movements in exchange rates. Foreign currency loans and advances are restricted to the availability of foreign currency deposits.

Notes (continued)

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

c) *Ensuring the availability of sufficient contingency liquidity;*

Funding markets are evaluated on an on-going basis to ensure appropriate Bank funding strategies are executed depending on the market, competitive and regulatory environment. The Bank employs a diversified funding strategy.

d) *Preserving a diversified funding base;*

Concentration risk limits are used within the Bank to ensure that funding diversification is maintained across products, sectors, and counterparties. Primary funding sources are in the form of deposits across a spectrum of retail and wholesale clients, as well as long-term capital.

e) *Undertaking regular liquidity stress testing;*

Stress testing and scenario analysis are based on hypothetical as well as historical events. These are conducted on the funding profiles and liquidity positions of the Bank. The crisis impact is typically measured over a two month period, as this is considered the most crucial time horizon for a liquidity event. Anticipated on- and off-balance sheet cash flows are subjected to a variety of bank-specific and systemic stresses and scenarios to evaluate the impact of unlikely but plausible events on liquidity positions. The results are assessed against the liquidity buffer and contingency funding plans to provide assurance as to the Bank's ability to maintain sufficient liquidity under adverse conditions.

f) *Maintaining adequate liquidity contingency plans or liquidity buffer;*

Portfolios of highly marketable securities over and above regulatory and stress testing requirements are maintained as protection against unforeseen disruptions in cash flows. These portfolios are managed within ALCO defined limits on the basis of diversification and liquidity.

g) *Short-term and long-term cash flow management;*

Active liquidity and funding management is an integrated effort across a number of functional areas. Short-term cash flow projections are used to plan for and meet the day-to-day requirements of the business, including adherence to prudential and internal requirements.

The Bank's long term funding strategy is derived from the projected net asset growth which includes consideration of Personal & Business Banking and Corporate & Investment Banking asset classes, capital requirements, the maturity profile of existing wholesale funding and anticipated changes in the retail deposit base. Funding requirements and initiatives are assessed in accordance with ALCO requirements for diversification, tenure and currency exposure, as well as the availability and pricing of alternative liquidity sources.

Liquidity contingency plans are designed to, as far as possible, protect stakeholder interests and maintain market confidence in the event of a liquidity crisis. The plans incorporate an extensive early warning indicator process supported by a clear and decisive crisis response strategy. Early warning indicators cover bank-specific and systemic crises and are monitored according to assigned frequencies and tolerance levels.

Crisis response strategies are formulated for the relevant crisis management structures and address internal and external communications and escalation processes, liquidity generation management actions and operations, and heightened and supplementary information requirements to address the crisis event.

The cumulative impact of the above elements is monitored on a monthly basis by the Bank's ALCO and the process is underpinned by a system of extensive internal and external controls. In periods of increased volatility, the frequency of meetings is increased as required to facilitate appropriate and timely management

To ensure integrity of the process there is use of application of purpose built technology, documented processes and procedures; independent oversight by risk management and regular independent reviews and evaluations of the effectiveness of the system. The total amount of liquidity held is adequate to meet all internal stress tests as well as regulatory requirements.

Notes (continued)

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

Exposure to liquidity risk

The key measure by the Bank for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose, 'net liquid assets' includes cash and cash equivalents and financial investment debt securities for which there is an active and liquid market less any deposits from banks. Details of the reported Bank ratio of net liquid assets to deposits from customers at the reporting date and during the reporting year were as follows:

	2018 %	2017 %
At 31 December	**54.3**	52.3
Average for the year	**58.0**	56.0
Maximum for the year	**65.8**	61.4
Minimum for the year	**58.0**	51.4
Statutory minimum requirement	**20.0**	20.0

The tables below present the remaining contractual maturities of the Bank's non-derivative financial liabilities; it includes a maturity analysis for financial assets that the Bank holds as part of managing liquidity risk – e.g. financial assets that are expected to generate cash inflows to meet cash outflows on financial liabilities.

The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Bank manages the inherent liquidity risk based on expected undiscounted cash inflows.

Notes (continued)

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

Maturity analysis for financial assets and financial liabilities

	Carrying value 2018 KShs'000	Gross nominal inflow/(outflow) 2018 KShs'000	Redeemable on demand 2018 KShs'000	Maturing within 1 month 2018 KShs'000	Maturing after 1 month but within 6 months 2018 KShs'000	Maturing after 6 months but within 12 months 2018 KShs'000	Maturing after 12 months but within 5 years 2018 KShs'000	Maturing After 5 years 2018 KShs'000
Non- derivative financial assets								
Cash and balances to banks	**22,061,875**	**22,061,875**	22,061,875	-	-	-	-	-
Financial assets held for trading	**31,202,035**	**33,052,574**	-	12,500	23,628,540	7,731,995	444,219	1,235,320
Financial assets at FVOCI	**17,851,517**	**18,461,684**	-	1,500,000	12,281,337	4,035,337	645,011	-
Financial assets at amortised cost	**23,200,956**	**32,416,353**	-	-	4,528,248	4,460,873	10,217,791	13,209,441
Loans and advances to banks	**28,294,576**	**28,313,879**	7,183,335	21,130,544	-	-	-	-
Loans and advances to customers	**146,604,117**	**175,384,482**	23,153,478	2,719,829	14,209,634	16,318,971	101,079,327	17,903,243
Other assets	**3,240,259**	**3,240,259**	3,240,259	-	-	-	-	-
	272,455,335	**312,931,107**	**55,638,947**	**25,362,873**	**54,647,759**	**32,547,176**	**112,386,348**	**32,348,004**
Derivative assets:	**1,515,466**							
- Inflows		**(490,620)**	-	(39,016)	(219,997)	(137,397)	(94,210)	-
- Outflows		**2,215,298**	-	167,428	527,514	247,515	762,123	510,718
	1,515,466	**1,724,678**	**-**	**128,412**	**307,516**	**110,118**	**667,913**	**510,718**
Non- derivative financial liabilities								
Amounts due to other banks	**(27,909,240)**	**(30,313,730)**	-	(903,228)	(4,516,140)	(5,419,368)	(19,474,993)	-
Customer deposits	**(192,258,013)**	**(192,660,301)**	(175,854,126)	(6,294,944)	(5,610,838)	(4,138,015)	(762,378)	-
Trading liabilities	**10,373,068**	**(10,639,878)**	-	(2,049,625)	(7,747,142)	(843,111)	-	-
Borrowings	**(7,064,013)**	**(8,982,749)**	-	(60,970)	(288,026)	(307,067)	(5,035,081)	(3,291,605)
Other liabilities	**(5,641,026)**	**(5,641,026)**	(5,641,026)	-	-	-	-	-
	(222,499,224)	**(248,237,685)**	**(181,495,152)**	**(9,308,767)**	**(18,162,146)**	**(10,707,561)**	**(25,272,452)**	**(3,291,605)**
Derivative liabilities:	**(1,881,658)**							
- Inflows		**373,804**	-	15,916	67,264	96,152	152,506	41,965
- Outflows		**-**	-	(170,592)	(705,316)	(629,985)	(561,514)	(418,714)
	(1,881,658)	**373,804**	**-**	**(154,676)**	**(638,052)**	**(533,832)**	**(409,007)**	**(376,750)**

Notes (continued)

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

Maturity analysis for financial assets and financial liabilities (continued)

	Carrying value 2017 KShs'000	Gross nominal inflow/(outflow) 2017 KShs'000	Redeemable on demand 2017 KShs'000	Maturing within 1 month 2017 KShs'000	Maturing after 1 month but within 6 months 2017 KShs'000	Maturing after 6 months but within 12 2017 KShs'000	Maturing after 12 months but within 5 years 2017 KShs'000	Maturing After 5 years 2017 KShs'000
Non- derivative financial assets								
Cash and balances to banks	**8,044,783**	8,044,783	8,044,783	-	-	-	-	-
Financial assets held for trading	**29,806,020**	47,181,804	-	1,020,222	13,403,902	12,863,743	17,796,848	2,097,089
Pledged assets -available –for-sale	**4,915,107**	5,521,225	-	-	626,913	2,626,913	2,267,400	-
Financial assets-available-for-sale	**36,073,667**	43,695,914	-	2,000,000	21,538,319	4,785,507	5,148,579	10,223,510
Financial assets-held-to-maturity	**5,444,178**	5,590,370	-	-	263,932	263,932	2,093,757	2,968,750
Loans and advances to banks	**12,640,509**	12,771,390	8,435,507	4,335,883	-	-	-	-
Loans and advances to customers	**130,535,810**	166,750,035	23,414,144	2,728,564	14,218,061	16,371,383	95,065,830	14,952,054
Other assets	**3,184,459**	3,184,459	3,184,459	-	-	-	-	-
	230,644,533	**292,739,980**	**43,078,893**	**10,084,669**	**50,051,127**	**36,911,478**	**122,372,414**	**30,241,403**
Derivative assets:	**2,391,101**							
- Inflows		4,048,590	-	401,116	1,321,742	890,084	922,757	512,890
- Outflows		(164,879)	-	(861)	(18,695)	(62,916)	(59,219)	(23,188)
	2,391,101	**3,883,711**	**-**	**400,255**	**1,303,047**	**827,168**	**863,538**	**489,702**
Non- derivative financial liabilities								
Amounts due to other banks	**(38,707,135)**	(40,314,246)	(3,534,670)	(4,517,078)	(7,480,047)	(6,506,198)	(12,471,123)	(5,805,129)
Customer deposits	**(155,405,963)**	(155,715,720)	(142,449,384)	(4,039,695)	(6,128,566)	(2,638,956)	(447,685)	(11,434)
Trading liabilities	**(362,630)**	(381,672)	-	(159,844)	(221,828)	-	-	-
Borrowings	**(3,989,243)**	(6,072,000)	-	-	(259,000)	(259,000)	(5,554,000)	-
Other liabilities	**(5,425,290)**	(5,425,290)	(5,425,290)	-	-	-	-	-
	(203,890,261)	**(207,908,928)**	**(151,409,344)**	**(8,716,617)**	**(14,089,441)**	**(9,404,154)**	**(18,472,808)**	**(5,816,563)**
Derivative liabilities:	**(2,427,563)**							
- Inflows		70,421	-	1,629	3,865	4,638	37,101	23,188
- Outflows		(3,179,730)	-	(179,335)	(860,151)	(785,378)	(841,976)	(512,890)
	(2,427,563)	**(3,109,309)**	**-**	**(177,706)**	**(856,286)**	**(780,740)**	**(804,875)**	**(489,702)**

Notes (continued)
4 Financial risk management (continued)

4.4 Liquidity risk (continued)

Maturity analysis for financial assets and financial liabilities (continued)

The amounts in the table above have been compiled as follows:

Type of financial	Basis on which amounts are compiled
Non-derivative financial liabilities and financial	Undiscounted cash flows which include interest payments
Issued financial guarantee contracts, and unrecognised loan	Earliest possible contractual maturity. For issued financial guarantee contracts, maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.
Derivative financial liabilities and financial assets held for risk management purpose	Contractual undiscounted cash flows. The amounts shown are the gross nominal inflows and outflows for derivatives that have simultaneous gross settlement (e.g. forward exchange contracts and currency swaps) and the net amounts for derivatives that are net settled.

As part of the management of liquidity risk arising from financial liabilities, the Bank holds liquid assets comprises cash and cash equivalents and debt securities issued by sovereigns which can be readily sold to meet liquidity requirements. In addition the Bank maintains lines of credit with other banks and holds unencumbered assets eligible for use as collateral with central banks.

4.5 Financial instruments subject to offsetting, enforceable master netting arrangements or similar agreements

The following table sets out the impact of offset, as well as financial assets and financial liabilities that are subject to enforceable master netting arrangement or similar agreement, irrespective of whether they have been offset in accordance with IAS 32, as required by IFRS 7R disclosure requirements. The gross amounts of financial asset and financial liabilities and their net amounts disclosed in the table below have been measured in the statement of financial position on the following bases:

- Derivative asset and liabilities – fair value;
- Loans and advances – amortised cost; and
- Customer deposits – amortised cost.

Notes (continued)

4 Financial risk management (continued)

4.5 Financial instruments subject to offsetting, enforceable master netting arrangements or similar agreements (continued)

	Gross amount of recognised financial assets	Gross amounts of recognised financial liabilities offset in statement of financial position	Net amounts of financial assets presented in the statement of financial position	Financial instruments, financial collateral and cash collateral received	Net amount
	2018	**2018**	**2018**	**2018**	**2018**
	KShs'000	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Assets					
Loans and advances to customers and banks (before impairment)	186,149,736	-	186,149,736	(1,331,651)	184,818,085
Derivative assets	1,515,466	-	1,515,466	-	1,515,466
	187,665,202	**-**	**187,665,202**	**(1,331,651)**	**186,333,551**
Liabilities					
Deposi	220,167,253	-	220,167,253	-	220,167,253
Derivative liabilities	1,881,658	-	1,881,658	-	1,881,658
	222,048,911	**-**	**222,048,911**	**-**	**222,048,911**

Notes (continued)

4 Financial risk management (continued)

4.5 Financial instruments subject to offsetting, enforceable master netting arrangements or similar agreements (continued)

	Gross amount of recognised financial assets	Gross amounts of recognised financial liabilities offset in statement of financial position	Net amounts of financial assets presented in the statement of financial position	Financial instruments, financial collateral and cash collateral received	Net amount
	2017	2017	2017	2017	2017
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Assets					
Loans and advances to customers and banks (before impairment)	148,527,602	-	148,527,602	(1,520,838)	147,006,764
Derivative assets	2,391,101	-	2,391,101	-	2,391,101
	150,918,703	**-**	**150,918,703**	**(1,520,838)**	**149,397,865**
Liabilities					
Deposits	194,113,098	-	194,113,098	-	194,113,098
Derivative liabilities	2,427,563	-	2,427,563	-	2,427,563
	196,540,661	**-**	**196,540,661**	**-**	**196,540,661**

Notes (continued)

4 Financial risk management (continued)

4.5 Financial instruments subject to offsetting, enforceable master netting arrangements or similar agreements (continued)

The ISDA* and similar master netting arrangements do not meet the criteria for offsetting in the statement of financial position. This is because they create for the parties to the agreement a right of set-off of recognised amounts that is enforceable only following an event of default, insolvency or bankruptcy of the bank or the counterparties following other predetermined events. In addition the bank and its counterparties do not intent to settle on a net basis or to realise the assets and the liabilities simultaneously.

The bank receives collateral in the form of cash in respect of lending.

The table below sets out the nature of agreement, and the types of rights relating to items which do not qualify for offset but that are subject to a master netting arrangement or similar agreement.

Financial instrument	Nature of	Basis on which amounts are compiled
Derivative assets and liabilities	ISDAs	The agreement allows for offset in the event of default.
Trading assets and trading liabilities	Global master repurchase	The agreement allows for offset in the event of default.
Loans and advances to banks	Banks Act	In the event of liquidation or bankruptcy, offset shall be enforceable subject to meeting Banks Act requirements.
Deposits and current accounts	Banks Act	In the event of liquidation or bankruptcy, offset shall be enforceable subject to meeting Banks Act requirements.

IAS 32 Financial Instruments: Presentation (IAS 32) requires financial assets and financial liabilities to be offset and the net amount presented in the statement of financial position when, and only when, the bank has a current legally enforceable right to set off recognised amounts, as well as the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

** An ISDA master agreement is a standard agreement used in over-the-counter derivatives transactions. The ISDA Master Agreement, published by the International Swaps and Derivatives Association (ISDA), is a document that outlines the terms applied to a derivatives transaction between two parties.*

Notes (continued)

5 Assets and liabilities at fair value

5.1 Fair value hierarchy of instruments measured at fair value

Valuation process

All financial instruments carried at fair value, regardless of classification, are marked to market using models that have been validated independently by the Bank's model validation unit and approved by the market risk methodologies committee. This control applies to both off-the-shelf models as well as those developed internally by the Bank. Further, all inputs into the valuation models are subject to independent price validation procedures carried out by the market risk unit. Such price validation is performed on at least a monthly basis and daily where possible given the liquidity of the underlying price inputs. Less liquid risk drivers, which are typically used to mark level 3 assets and liabilities to market, are carefully validated and tabled at the monthly price validation forum to ensure these are reasonable and used consistently. Sensitivities arising from exposures to such drivers are similarly scrutinised, together with movements in level 3 fair values. They are also disclosed on a monthly basis to the market risk committee and ALCO.

Level hierarchy

The table that follows analyses financial instruments carried at fair value, by level of fair value hierarchy. The different levels are based on the extent that available market data is used in the calculation of the fair value of the financial instruments. The levels have been defined as follows:

Level 1 – fair value is based on quoted market prices (unadjusted) in active markets for identical instruments.

Level 2 – fair value is determined through valuation techniques based on observable inputs, either directly, such as quoted prices, or indirectly, such as derived from quoted prices. This category includes instruments valued using quoted market prices in active markets for similar instruments, quoted prices for identical or similar instruments in markets that are considered less than active or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3 – fair value is determined through valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the assets and liabilities.

Significant unobservable inputs

The fair value of level 3 assets and liabilities is determined using valuation techniques that include reference to recent arm's length transactions, discounted cash flow analyses, pricing models and other valuation techniques commonly used by market participants. However, such techniques typically have unobservable inputs that are subject to management judgement. These inputs include credit spreads on illiquid issuers, implied volatilities on thinly traded stocks, correlation between risk factors, prepayment rates and other illiquid risk drivers. Exposure to such illiquid risk drivers is typically managed by:

- using bid-offer spreads that are reflective of the relatively low liquidity of the underlying risk driver;
- raising day one profit provisions in accordance with IFRS;
- quantifying and reporting the sensitivity to each risk driver; and
- limiting exposure to such risk drivers and analysing this exposure on a regular basis.

Notes (continued)

5 Assets and liabilities at fair value

5.2 Assets and liabilities measured at fair value on a recurring basis

The table below analyses financial instruments carried at fair value, by level of fair value hierarchy:

At 31 December 2018	Note	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Total KShs'000
Assets					
Cash and balances with the Central Bank of Kenya (minimum regulatory reserve)	19	11,041,606	-	-	11,041,606
Financial assets – held for trading	21	-	31,202,035	-	31,202,035
Financial assets – FVOCI	22	-	17,851,517	-	17,851,517
Equity investments	23	-	-	17,500	17,500
Derivative assets	24	-	1,515,466	-	1,515,466
		11,041,606	**50,569,019**	**17,500**	**61,628,125**
Liabilities					
Trading liabilities	21	-	10,373,068	-	10,373,068
Derivative liabilities	24	-	1,881,658	-	1,881,658
		-	**12,254,726**	**-**	**12,254,726**

At 31 December 2017	Note		Level 2 KShs'000		Total KShs'000
Assets					
Financial assets – held for trading	21	-	29,806,020	-	29,806,020
Financial assets – available-for-sale	22	-	36,073,667	-	36,073,667
Pledged assets – available-for-sale	23	-	4,915,107	-	4,915,107
Derivative assets	24	-	2,391,101	-	2,391,101
		-	**73,185,895**	**-**	**73,185,895**
Liabilities					
Trading liabilities	21	-	362,630	-	362,630
Derivative liabilities	24	-	2,427,563	-	2,427,563
		-	**2,790,193**	**-**	**2,790,193**

There were no transfers between levels in 2018 and 2017.

Fair value of level 2 financial instruments

The fair value of level 2 financial instruments is determined using valuation techniques which incorporate assumptions that are indirectly supported by prices from observable current market transactions in the same instruments and are based on available observable market data. Such assumptions include risk premiums, liquidity discount rates, credit risk, volatilities and correlations. Changes in these assumptions could affect the reported fair values of these financial instruments.

Notes (continued)

5 Assets and liabilities at fair value

5.2 Assets and liabilities measured at fair value on a recurring basis (continued)

Level 2 financial assets and financial liabilities

2018	Valuation basis/technique	Main assumptions[1]
Derivative instruments	Discounted cash flow model Black-Scholes model Multiple valuation technique	Discount rate Risk-free rate, volatility rate Valuation multiples
Trading assets	Discounted cash flow model Black-Scholes model	Discount rate, liquidity discount rate Risk-free rate, volatility rate
Pledged assets	Discounted cash flow model	Discount rate, liquidity discount rate
Financial instruments	Discounted cash flow model Multiple valuation technique Quoted exit price adjusted for notice period	Discount rate, liquidity discount rate Valuation multiples Discount rate
Cash with Central Bank of Kenya	Prevailing exchange rate	Exchange rate
Investment in equities	Sale price	Discount rate

[1] *The main assumptions for all instruments include applicable credit spreads.*

Notes (continued)

5 Assets and liabilities at fair value

5.3 Assets and liabilities not measured at fair value

Financial assets and financial liabilities

The fair value hierarchy for financial assets not measured at fair value is as shown in the table below:

	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Fair value KShs'000	KShs'000
At 31 December 2018					
Assets					
Cash and balances with the Central Bank of Kenya (Note 19)	11,020,269	-	-	11,020,269	11,020,269
Financial investments – Amortised cost	-	32,301,824	-	32,301,824	23,200,956
Loans and advances to banks	-	-	28,277,822	28,277,822	28,294,576
Loans and advances to customers	-	-	162,757,149	162,757,149	146,604,117
Other assets	-	-	3,240,259	3,240,259	3,240,259
	11,020,269	**32,301,824**	**194,275,230**	**237,597,323**	**212,360,177**
Liabilities					
Deposits from customers	-	-	(192,494,661)	(192,494,661)	(192,258,013)
Deposits from banks	-	-	(30,216,470)	(30,216,470)	(27,909,240)
Borrowings	-	-	(9,010,645)	(9,010,645)	(7,064,013)
Other liabilities	-	-	(5,641,026)	(5,641,026)	(5,641,026)
	-	**-**	**(237,362,802)**	**(237,362,802)**	**(232,872,292)**

	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Fair value KShs'000	Carrying value KShs'000
At 31 December 2017					
Assets					
Cash and balances with CBK	8,044,783	-	-	-	8,044,783
Loans and advances to banks	-	-	12,767,058	12,767,058	12,640,509
Loans and advances to customers	-	-	147,236,355	147,236,355	130,535,810
Financial assets – held-to-maturity	-	5,590,370	-	5,590,370	5,444,178
Other assets	-	-	3,184,459	3,184,459	3,184,459
	8,044,783	**5,590,370**	**163,187,872**	**168,778,242**	**159,849,739**
Liabilities					
Deposits from banks	-	-	(40,314,246)	(40,314,246)	(38,707,135)
Deposits from customers	-	-	(155,715,720)	(155,715,720)	(155,405,963)
Borrowings	-	-	(5,617,021)	(5,617,021)	(3,989,243)
Other liabilities	-	-	(5,425,290)	(5,425,290)	(5,425,290)
	-	**-**	**(207,072,277)**	**(207,072,277)**	**(203,527,631)**

The valuation techniques used in determining the fair value of financial assets and liabilities classified within level 2 and level 3.

The table below indicates the valuation techniques and main assumptions used in the determination of the fair value of the level 2 and level 3 assets and liabilities not measured at fair value but for which fair value is disclosed:

2018	Valuation basis/technique	Main assumptions
Loans and advances to banks	Discounted cash flow model	Discount rate, liquidity discount rate
Loans and advances to customers	Discounted cash flow model	Discount rate, liquidity discount rate
Deposits from banks	Discounted cash flow model	Discount rate, liquidity discount rate
Deposits from customers	Discounted cash flow model	Discount rate, liquidity discount rate
Subordinated debt	Discounted cash flow model	Discount rate, liquidity discount rate
Other financial assets	Discounted cash flow model	Discount rate, liquidity discount rate
Other financial liabilities	Discounted cash flow model	Discount rate, liquidity discount rate

Notes (continued)

6 Segment information

The Bank is required to disclose information to the users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates in compliance with IFRS 8.

An operating segment is a component of the Bank engaged in business activities, whose operating results are reviewed regularly by management in order to make decisions about resources to be allocated to segments and assessing segment performance. Identification of segments and the measurement of segment results is based on the Bank's internal reporting to management.

The Chief Executive with the assistance of the Executive Committee (EXCO) and the Asset and Liability Committee (ALCO) is the Bank's chief operating decision-maker. The directors have determined the operating segments based on the reports reviewed by the chief operating decision-maker that are used to make strategic decisions. Management considers the business from client turnover perspective.

The Bank has therefore segmented its operations into two, Personal and Business Banking (PBB) and Corporate and Investment Banking (CIB).

Personal and Business Banking (PBB)

PBB provides banking and other financial services to individual customers and small to medium sized enterprises. The products offered include:

- Mortgage lending – provides residential accommodation loans to individual customers.
- Instalment sales and finance leases – comprises two areas, instalment finance in the consumer market, mainly vehicles, and secondly, finance of vehicles and equipment in the business market.
- Card products – provides card facilities to individuals and businesses.
- Transactional and lending products – transactions in products associated with the various points of contact channels such as ATMs, Internet, and branches. This includes deposit taking activities, electronic banking, cheque accounts and other lending products.

Corporate and Investment Banking (CIB)

CIB provides commercial and investment banking services to larger corporates, financial institutions, and international counter-parties. The products offered include:

- Global Markets – includes foreign exchange and debt securities trading.
- Transactional products and services – includes transactional banking and investor services.
- Investment Banking – includes project finance, advisory, structured finance, structured trade finance, corporate lending, primary markets and property finance.

Major Customers

The Bank does not have any one major customer that contributes more than 10% of the Bank's revenues. However, the Bank has one major customer whose deposits contribute 10.7% of total deposits as at December 2018 (2017: 9.9%). The interest expense paid to this customer is reported under the Corporate and Investment Banking segment.

Notes (continued)

6 Segment information (continued)

The segment financial results are as follows:

Income statement	Total KShs'000 2018	Total KShs'000 2017	CIB KShs'000 2018	CIB KShs'000 2017	PBB KShs'000 2018	PBB KShs'000 2017
Interest income	19,209,386	16,592,500	11,284,087	9,512,287	7,925,299	7,080,213
Interest expense	(7,157,013)	(6,004,664)	(4,932,370)	(3,839,711)	(2,224,643)	(2,164,953)
Net interest income	**12,052,373**	**10,587,836**	**6,351,717**	**5,672,576**	**5,700,656**	**4,915,260**
Credit impairment losses	(2,064,462)	(2,761,325)	(809,143)	(1,982,801)	(1,255,319)	(778,524)
Net income after credit impairment losses	**9,987,911**	**7,826,511**	**5,542,574**	**3,689,775**	**4,445,336**	**4,136,736**
Fees and commission income	4,445,085	3,947,733	1,941,363	1,796,246	2,503,722	2,151,487
Fees and commission expense	(430,944)	(401,215)	(114,234)	(121,364)	(316,710)	(279,851)
Net fees and commission income	**4,014,141**	**3,546,518**	**1,827,129**	**1,674,882**	**2,187,012**	**1,871,636**
Trading income	5,391,607	4,403,262	5,391,607	4,403,135	-	127
Net other operating income	19,299	109,980	14,393	66,050	4,906	43,930
Net trading and other income	**5,410,906**	**4,513,242**	**5,406,000**	**4,469,185**	**4,906**	**44,057**
Total income	**19,412,958**	**15,886,271**	**12,775,703**	**9,833,842**	**6,637,255**	**6,052,429**
Employee benefits expense	(5,651,978)	(5,569,321)	(2,313,307)	(2,378,495)	(3,338,671)	(3,190,826)
Depreciation and amortisation expense	(607,217)	(557,245)	(224,025)	(304,020)	(383,192)	(253,225)
Administrative expenses	(4,274,966)	(4,063,303)	(2,207,534)	(2,006,089)	(2,067,432)	(2,057,214)
Finance costs	(93,579)	(283,452)	(92,746)	(283,452)	(833)	-
Profit before income tax	**8,785,218**	**5,412,950**	**7,938,090**	**4,861,786**	**847,128**	**551,164**
Income tax expense	(2,609,146)	(1,073,814)	(2,322,139)	(888,840)	(287,007)	(184,974)
Profit for the year	**6,176,072**	**4,339,136**	**5,615,951**	**3,972,946**	**560,121**	**366,190**

Notes (continued)

6 Segment information (continued)

Statement of financial position	Total KShs'000 2018	Total KShs'000 2017	CIB KShs'000 2018	CIB KShs'000 2017	PBB KShs'000 2018	PBB KShs'000 2017
Assets						
Cash and balances with Central Bank of Kenya	#VALUE!	8,044,783	#VALUE!	4,494,062	#VALUE!	3,550,721
Financial investments	#VALUE!	76,238,972	#VALUE!	76,238,972	#VALUE!	-
Pledged assets	#VALUE!	4,915,107	#VALUE!	4,915,107	#VALUE!	-
Derivative assets	#VALUE!	2,391,101	#VALUE!	2,391,101	#VALUE!	-
Loans and advances to banks	#VALUE!	12,640,509	#VALUE!	12,640,509	#VALUE!	-
Loans and advances to customers	#VALUE!	130,535,810	#VALUE!	66,066,028	#VALUE!	64,469,782
Investment in subsidiary	#VALUE!	2	#VALUE!	2	#VALUE!	-
Other investments	#VALUE!	17,500	17,500	17,500	#VALUE!	-
Property, equipment and intangibles	#VALUE!	3,385,933	#VALUE!	1,884,003	#VALUE!	1,501,930
Deferred income tax	#VALUE!	2,488,760	#VALUE!	1,631,981	#VALUE!	856,779
Current income tax	#VALUE!	16,667	#VALUE!	16,667	#VALUE!	-
Other assets	#VALUE!	3,647,838	#VALUE!	172,311	#VALUE!	3,475,527
Total assets	**#VALUE!**	**244,322,982**	**#VALUE!**	**170,468,243**	**#VALUE!**	**73,854,739**
Liabilities						
Customer deposits	192,258,013	155,405,963	101,937,101	85,253,539	90,320,912	70,152,424
Amounts due to other banks	27,909,240	38,707,135	27,909,240	38,707,135	-	-
Current income tax	1,097,202	-	790,171	-	307,031	-
Deferred tax liability	-	38,859	-	38,859	-	-
Trading liabilities	10,373,068	362,630	10,373,068	362,630	-	-
Derivative liabilities	1,881,658	2,427,563	1,868,003	2,427,563	13,655	-
Borrowings	7,064,013	3,989,242	1,737,539	2,444,966	5,326,474	1,544,276
Other liabilities	5,779,102	5,425,291	3,124,275	3,089,489	2,654,827	2,335,802
Total liabilities	**246,362,296**	**206,356,683**	**147,739,397**	**132,324,181**	**98,622,899**	**74,032,502**
Shareholders' equity	**34,590,716**	**33,051,193**	**20,416,792**	**20,694,056**	**14,173,924**	**12,357,137**
Funding	-	-	28,374,708	12,534,900	(28,374,708)	(12,534,900)
Total equity and liabilities	**280,953,012**	**239,407,876**	**196,530,897**	**165,553,137**	**84,422,115**	**73,854,739**

Notes (continued)

6 Segment information (continued)

The Bank is domiciled in Kenya and the revenue and non-current assets by country of domicile are included in the sections below:

Income statement	**Total KShs'000 2018**	**Total KShs'000 2017**	**Kenya KShs'000 2018**	**Kenya KShs'000 2017**	**South Sudan KShs'000 2018**	**South Sudan KShs'000 2017**
Interest income	19,209,386	16,592,500	19,207,763	16,591,346	1,623	1,154
Interest expense	(7,157,013)	(6,004,664)	(7,150,228)	(6,001,203)	(6,785)	(3,461)
Net interest income	**12,052,373**	**10,587,836**	**12,057,535**	**10,590,143**	**(5,162)**	**(2,307)**
Credit impairment losses	(2,064,462)	(2,761,325)	(2,113,139)	(3,009,644)	48,677	248,319
Net income after credit impairment losses	**9,987,911**	**7,826,511**	**9,944,396**	**7,580,499**	**43,515**	**246,012**
Fees and commission income	4,445,085	3,947,732	3,753,711	3,359,272	691,374	588,460
Fees and commission expense	(430,944)	(401,215)	(427,266)	(396,089)	(3,678)	(5,126)
Net fees and commission income	**4,014,141**	**3,546,517**	**3,326,445**	**2,963,183**	**687,696**	**583,334**
Trading revenue	5,350,669	4,403,262	4,910,095	3,943,227	440,574	460,035
Net income from financial instruments at FVPL	40,938	-	40,807	-	131	-
Other income	18,408	109,980	18,404	109,974	4	6
Other gains and losses on financial instruments1	891	-	891	-	-	-
Net trading and other income	**5,410,906**	**4,513,242**	**4,970,197**	**4,053,201**	**440,709**	**460,041**
Total income	**19,412,958**	**15,886,270**	**18,241,038**	**14,596,883**	**1,171,920**	**1,289,387**
Employee benefits expense	(5,651,978)	(5,569,320)	(5,339,829)	(5,289,033)	(312,149)	(280,288)
Depreciation	(607,217)	(557,245)	(602,961)	(551,286)	(4,256)	(5,959)
Other operating expenses	(4,274,966)	(4,063,303)	(3,921,783)	(3,671,738)	(353,183)	(391,565)
Finance costs	(93,579)	(283,452)	(54,156)	(56,448)	(39,423)	(227,004)
Profit before income tax	**8,785,218**	**5,412,950**	**8,322,311**	**5,028,380**	**462,909**	**384,570**
Income tax expense	(2,609,146)	(1,073,814)	(2,543,243)	(1,047,611)	(65,903)	(26,203)
Profit for the year	**6,176,072**	**4,339,136**	**5,779,068**	**3,980,769**	**397,006**	**358,367**

Notes (continued)

6 Segment information (continued)

Statement of financial position	Total KShs'000 2018	Total KShs'000 2017	Kenya KShs'000 2018	Kenya KShs'000 2017	South Sudan KShs'000 2018	South Sudan KShs'000 2017
Assets						
Cash and balances with Central Bank of Kenya	23,951,804	8,966,331	21,951,949	7,946,940	1,999,855	1,019,391
Financial investments	72,254,508	76,238,972	72,254,508	76,238,972	-	-
Derivative assets	1,515,466	2,391,101	1,515,466	2,391,055	-	46
Loans and advances to banks	38,673,963	19,741,699	25,349,856	8,522,015	13,324,107	11,219,684
Loans and advances to customers	146,604,117	130,543,605	146,591,893	130,538,886	12,224	4,719
Investment in subsidiary	2	2	2	2	-	-
Other investments	17,500	17,500	17,500	17,500	-	-
Property, equipment and intangibles	3,266,867	3,385,933	3,186,270	3,323,109	80,597	62,824
Deferred income tax	3,205,907	2,488,760	3,196,687	2,488,760	9,220	-
Current income tax	-	16,667	-	(2,697)	-	19,364
Other assets	6,303,152	6,050,013	6,256,379	5,992,333	46,773	57,679
Total assets	**295,793,286**	**249,840,583**	**280,320,510**	**237,456,875**	**15,472,776**	**12,383,707**
Liabilities						
Customer deposits	192,258,013	155,405,963	181,626,421	147,392,539	10,631,592	8,013,424
Amounts due to other banks	40,177,886	46,759,668	39,091,045	45,941,810	1,086,841	817,858
Current income tax	1,097,202	-	1,032,814	-	64,388	-
Deferred tax liability	-	38,859	-	-	-	38,859
Trading liabilities	10,373,068	362,630	10,373,068	362,630	-	-
Derivative liabilities	1,881,658	2,427,563	1,881,658	2,427,562	-	1
Borrowings	7,064,013	3,989,243	7,064,013	3,989,243	-	-
Other liabilities	8,350,730	7,805,571	5,573,571	5,076,254	2,777,159	2,729,317
Total liabilities	**261,202,570**	**216,789,497**	**246,642,590**	**205,190,038**	**14,559,980**	**11,599,459**
Shareholders' equity	**34,590,716**	**33,051,086**	**33,677,919**	**32,266,837**	**912,797**	**784,248**
Total equity and liabilities	**295,793,286**	**249,840,583**	**280,320,509**	**237,456,875**	**15,472,777**	**12,383,707**

Notes (conntinued)

6 Segment information (continued)

Reconciliation of reportable assets and liabilities:

	2018 KShs'000	2017 KShs'000
Assets		
Total assets for reportable segments	295,793,286	249,840,583
Elimination of inter-branch balances	(14,840,274)	(10,432,706)
Entity's total assets	**280,953,012**	**239,407,877**
Liabilities		
Total liabilities for reportable segments	295,793,286	249,840,583
Elimination of inter-branch balances	(14,840,274)	(10,432,706)
Entity's total liabilities	**280,953,012**	**239,407,877**

7 Interest income

	2018 KShs'000	2017 KShs'000
Loans and advances to customers	14,529,796	12,061,634
Financial assets – (FVOCI/available-for-sale)	2,361,492	4,146,647
Financial investments – (amortised cost/held to maturity)	1,982,526	120,823
Loans and advances to banks	335,572	263,396
Total interest income	**19,209,386**	**16,592,500**
Interest expense		
Current accounts	1,222,518	718,977
Savings and term deposit accounts	3,316,399	3,025,589
Deposits and placements from other banks	1,935,371	1,738,995
Interest on borrowed funds	682,725	521,103
Total interest expense	**7,157,013**	**6,004,664**
Net interest income	**12,052,373**	**10,587,836**

All interest income reported above relates to financial assets not carried at fair value through profit or loss and all interest expense reported relates to financial liabilities not carried at fair value through profit or loss.

8 Fees and commission income

	2018 KShs'000	2017 KShs'000
Points of representation transaction fees	1,467,274	1,364,743
Documentation and administration fees	286,904	304,349
Electronic banking fees	545,982	372,899
Knowledge based fees and commission	1,309,297	1,177,103
Card based commission	247,863	182,963
Foreign service fees	540,178	510,838
Other bank related fees and commission	47,587	34,838
	4,445,085	**3,947,733**

Notes (conntinued)

9 Fees and commission expense

	2018 KShs'000	2017 KShs'000
Points of representation transaction expenses	97,312	69,010
Card based commission expenses	165,407	104,222
Other bank related fees and commission expenses	168,225	227,983
	430,944	**401,215**

Other bank related fees and commission relates to card courier fees.

The net fees and commission earned by the Bank on trust and fiduciary activities where the Bank holds or invests assets on behalf of its customers is KShs 305,885,000 (2017: KShs 268,413,000).

All net fee and commission revenue reported above relates to financial assets or liabilities not carried at fair value through profit or loss.

10 Trading revenue

	2018 KShs'000	2017 KShs'000
Net foreign exchange income	5,350,669	3,826,785
	5,350,669	**3,826,785**

11 Net income from financial instruments at fair value through profit and loss

	2018 KShs'000	2017 KShs'000
Fixed income – financial assets – held for trading	40,938	576,477
	40,938	**576,477**

12 Other operating income

Gain on disposal of subsidiary	-	42,164
Interest recovered from Bank receivables	-	46,240
Other income	18,408	21,576
	18,408	**109,980**

13 Employee benefits expense

Salaries and wages	5,260,038	5,191,264
Retirement benefit costs	391,940	378,057
	5,651,978	**5,569,321**
Included in retirement benefit costs are;		
Defined contribution scheme	389,084	374,999
National Social Security Fund	2,855	3,058
	391,940	**378,057**
Staff numbers		
Management	346	310
Supervisory	480	510
Clerical	222	232
Other categories	40	66
Total	**1,088**	**1,118**

Notes (conntinued)

14 Breakdown of expenses by nature

	Note	2018 KShs'000	2017 KShs'000
Profit before tax has been arrived at after			
Employees benefit	13	5,651,978	5,569,321
Audit fees		20,855	20,608
Directors' fees		31,633	26,384
Depreciation of property and equipment	30	415,413	378,665
Amortisation of intangible assets	31	191,804	178,580

15 Finance costs

	2018 KShs'000	2017 KShs'000
Bank charges	84,163	96,950
Loss in monetary value	9,416	186,502
	93,579	**283,452**

16 Income tax expense

	2018 KShs'000	2017 KShs'000
Current income tax	**2,660,743**	**2,061,861**
Current year charge (credit)/ debit (Note 33 (a))	2,905,059	2,061,861
Previous year current income tax over-provision	(244,316)	-
Deferred income tax	**(51,597)**	**(988,047)**
Current year charge asset (credit)/ debit (Note 32 (a))	(619,232)	(1,014,112)
Previous year deferred income tax under-provision	606,494	-
Current year charge liability (credit)/ debit (Note 32 (b))	(38,859)	26,064
Income tax expense	**2,609,146**	**1,073,814**

Reconciliation of tax expense to expected tax base based on accounting profit:

The tax on the profit before tax differs from the theoretical amount using the statutory income tax rate as follows:

	2018 KShs'000	2017 KShs'000
Profit before income tax	**8,785,218**	**5,412,950**
Tax at statutory tax rate of 30% (2017: 30%)	2,635,565	1,623,885
Tax effect of:		
Income not subjected to tax	(596,900)	(702,485)
Expenses not deductible for tax purposes	143,915	162,354
Previous year current income tax over-provision	(244,316)	-
Previous year deferred income tax under-provision	606,494	-
Effect of different tax rate in South Sudan	64,388	(9,940)
Income tax expense	**2,609,146**	**1,073,814**

Notes (conntinued)

17 Earnings per share – basic and diluted

Basic earnings per share are calculated by dividing the profit attributable to equity holders of the company by the weighted average number of ordinary shares in issue during the year.

	2018	2017
Earnings (Profit after tax)		
Earnings for the purposes of basic earnings per share (KShs'000)	6,176,072	4,339,136
Number of shares		
Weighted average number of ordinary shares for the purpose of basic earnings per share (in thousands)	170,577	170,577
Earnings per share (KShs) basic and diluted	**36.21**	**25.44**

There were no potentially dilutive shares as at 31 December 2018 or 31 December 2017.

Therefore, diluted earnings per share are the same as basic earnings per share.

18 Dividend

	2018	2017
The calculation of dividends per share is based on:		
Dividends for the year attributable to ordinary shareholders:		
Interim dividend paid (KShs‘000)	900,000	500,000
Final dividend proposed (KShs‘000)	1,300,000	1,600,000
	2,200,000	**2,100,000**
Number of ordinary shares at issue date (thousands)	170,577	170,577
Dividends per share – KShs	**12.90**	**12.31**

Proposed dividends are accounted for as a separate component of equity until they have been ratified at an Annual General Meeting.

At the Annual General Meeting to be held on 9th May 2019, a final dividend per share in respect of the year ended 31 December 2018 of KShs 7.62 (2017: KShs 9.38) per share amounting to a total of KShs 1,300,000,000 (2017: KShs 1,600,000,000) is to be proposed. These financial statements do not reflect this dividend payable, the proposed dividend has however been transferred to a separate category of equity.

During the year an interim dividend per share of KShs 5.28 (2017: KShs 2.93) per share, amounting to a total of KShs 900,000,000 (2017: KShs 500,000,000) was paid. The total dividend for the year is therefore KShs 12.90 (2017: KShs 12.31) amounting to a total of KShs 2,200,000,000 (2017: KShs 2,100,000,000).

Payment of dividends is subject to withholding tax at a rate of either 10% or 15% depending on the residence of the respective shareholders.

Notes (conntinued)

19 Classification of assets and liabilities

Accounting classifications and fair values of assets and liabilities

The table below categorises the Bank's assets and liabilities as at 31 December 2018 between those that are financial and non-financial.

All financial assets and liabilities have been classified according to their measurement category with disclosure and their fair value.

Year ended 31 December 2018	Fair value through profit and loss - default KShs'000	Fair value through profit or loss - designated KShs'000	Amortised cost KShs'000	Fair value through OCI KShs'000	Other non-financial assets/liabilities	Total carrying amount KShs'000	Fair value KShs'000
Assets							
Cash and balances with Central Bank of Kenya	-	11,041,606	11,020,269	-	-	**22,061,875**	22,061,875
Financial assets – held for trading	31,202,035	-	-	-	-	**31,202,035**	31,202,035
Financial assets – FVOCI	-	-	-	17,851,517	-	**17,851,517**	17,851,517
Financial assets – amortised cost	-	-	23,200,956	-	-	**23,200,956**	32,301,824
Derivative assets	1,515,466	-	-	-	-	**1,515,466**	1,515,466
Loans and advances to banks	-	3,052,017	25,242,559	-	-	**28,294,576**	28,277,822
Loans and advances to customers	-	-	146,604,117	-	-	**146,604,117**	162,757,149
Other financial assets	-	-	3,732,194	-	-	**3,732,194**	3,732,194
Investment securities	17,500	-	-	-	-	**17,500**	17,500
Other non - financial assets	-	-	-	-	6,490,276	**6,490,276**	-
	32,735,001	**14,093,623**	**209,800,095**	**17,851,517**	**6,490,276**	**280,970,512**	**299,717,382**
Liabilities							
Deposits from customers	-	-	(192,258,013)	-	-	**(192,258,013)**	(192,494,661)
Deposits from banks	-	-	(27,909,240)	-	-	**(27,909,240)**	(30,216,470)
Derivative liabilities	(1,881,658)	-	-	-	-	**(1,881,658)**	(1,881,658)
Trading liabilities	(10,373,068)	-	-	-	-	**(10,373,068)**	(10,373,068)
Borrowings	-	-	(7,064,013)	-	-	**(7,064,013)**	(9,010,645)
Other financial liabilities	-	-	(5,779,102)	-	-	**(5,779,102)**	(5,779,102)
Other non - financial liabilities	-	-	-	-	(1,097,202)	**(1,097,202)**	-
	(12,254,726)	**-**	**(233,010,368)**	**-**	**(1,097,202)**	**(246,362,296)**	**(249,755,604)**

Notes (conntinued)
19 Classification of assets and liabilities (continued)

Accounting classifications and fair values of assets and liabilities (continued)

Year ended 31 December 2017	Held for Trading KShs'000	Loans and receivables KShs'000	Available-for-sale KShs'000	Amortised cost KShs'000	Other non-financial assets/liabilities KShs'000	Total carrying amount KShs'000	Fair value KShs'000
Assets							
Cash and balances with Central Bank of Kenya	-	8,044,783	-	-	-	8,044,783	8,044,783
Financial assets – held for trading	29,806,020	-	-	-	-	29,806,020	29,806,020
Financial assets - held to maturity	-	-	-	5,444,178	-	5,444,178	5,401,894
Financial assets – available-for-sale	-	-	36,073,667	-	-	36,073,667	36,073,667
Pledged assets– available-for-sale	-	-	4,915,107	-	-	4,915,107	4,915,107
Derivative assets	2,391,101	-	-	-	-	2,391,101	2,391,101
Loans and advances to banks	-	12,640,509	-	-	-	12,640,509	12,771,390
Loans and advances to customers	-	130,535,810	-	-	-	130,535,810	166,750,035
Other financial assets	-	3,647,838	-	-	-	3,647,838	3,647,838
Investment securities	17,500	-	-	-	-	17,500	17,500
Other non - financial assets	-	-	-	-	5,860,539	5,860,540	-
	32,214,621	**154,868,940**	**40,988,774**	**5,444,178**	**5,860,539**	**239,377,053**	**269,819,335**
Liabilities							
Customer deposits	-	-	-	(155,405,963)	-	(155,405,963)	(155,715,720)
Amounts due to other banks	-	-	-	(37,831,417)	-	(37,831,417)	(40,314,246)
Derivative liabilities	(2,427,563)	-	-	-	-	(2,427,563)	(2,427,563)
Trading liabilities	(362,630)	-	-	-	-	(362,630)	(362,630)
Borrowings	-	-	-	(3,989,299)	-	(3,989,299)	(6,072,000)
Other financial liabilities	-	-	-	(5,425,398)	-	(5,425,398)	(5,425,398)
Other non - financial liabilities	-	-	-	-	(38,859)	(38,859)	-
	(2,790,193)	**-**	**-**	**(202,652,077)**	**(38,859)**	**(205,481,129)**	**(210,317,557)**

Notes (continued)

20 Cash and balances with Central Bank of Kenya

	2018 KShs'000	2017 KShs'000
Cash in hand	2,024,503	1,586,469
Balances with Central Bank of Kenya	20,037,372	6,458,314
	22,061,875	**8,044,783**

Banks are required to maintain a prescribed minimum cash reserve ratio (CRR) including cash in hand and balances with Central Bank of Kenya. The minimum cash reserve is non-interest earning and is based on the value of deposits as adjusted for Central Bank of Kenya requirements. At 31 December 2018, the cash reserve requirement was 5.25% of the eligible deposits (2017: 5.25%).

The cash reserve requirement balance for the year ended 31 December 2018 is KShs 9,017,102,168 (2017: KShs 7,459,981,410).The Central Bank allows a daily minimum of 3% (2017: 3%) of CRR when the average total reserving for the month is above Kshs 5,250,000,000. The Bank therefore held Kshs 5,152,629,810 as at 31 December 2018 (2017: KShs 4,340,522,340) to fulfil this prudential requirement.

21 Financial assets and liabilities held for trading

a) Financial assets – held for trading	2018 KShs'000	2017 KShs'000
Government treasury bills and bonds	31,202,021	29,805,992
Corporate bonds	14	28
	31,202,035	**29,806,020**
Maturity analysis		
Maturing within 1 month	-	998,307
Maturing after 1 month but within 6 months	23,059,441	12,674,151
Maturing after 6 months but within 12 months	7,196,326	12,176,738
Maturing after 12 months	946,268	3,956,824
	31,202,035	**29,806,020**

The maturities represent periods to contractual redemption of trading assets recorded. Trading assets had a redemption value at 31 December 2018 of KShs 32,147,772,000 (2016: KShs 30,622,707,000). The weighted average effective interest yield on debt securities held for trading at 31 December 2018 was 10.28% (2017: 10.51%).

b) Financial liabilities - held for trading	2018 KShs'000	2017 KShs'000
Unlisted	10,373,068	362,630
	10,373,068	**362,630**
Maturity analysis		
Maturing within 1 month	1,679,175	152,965
Maturing after 1 month but within 6 months	7,844,401	209,665
Maturing after 6 months but within 12 months	849,492	-
	10,373,068	**362,630**

The maturities represent periods to contractual redemption of trading liabilities recorded. Dated trading liabilities had a redemption value at 31 December 2018 of KShs 10,296,401,000 (2017: KShs 358,794,000). The weighted average effective interest cost on debt securities held for trading at 31 December 2018 was 6.91% (2017: 5.64%).

Notes (continued)

22 Financial investments – (FVOCI/available-for-sale)

	2018 KShs'000	2017 KShs'000
Financial assets – (FVOCI/available-for-sale)	15,988,475	36,073,667
Pledged assets – (FVOCI/available-for-sale)	1,863,042	4,915,107
	17,851,517	**40,988,774**

22 (a) Financial assets – (FVOCI/available-for-sale)

	2018 KShs'000	2017 KShs'000
Debt securities – at fair value:		
Listed	2,374,913	10,407,312
Unlisted	13,613,562	25,666,355
	15,988,475	**36,073,667**
Comprising:		
Government bonds	2,374,913	10,409,256
Government treasury bills	13,613,562	25,664,411
	15,988,475	**36,073,667**

Maturity analysis	2018 KShs'000	2017 KShs'000
Maturing within 1 month	1,465,376	1,989,504
Maturing after 1 month but within 6 months	12,062,516	20,409,920
Maturing after 6 months but within 12 months	1,879,025	4,040,152
Maturing after 12 months but within 5 years	581,558	9,634,091
	15,988,475	**36,073,667**

Financial investment securities had a redemption value at 31 December 2018 of KShs 16,285,000,000 (2017: KShs 36,628,247,000).

22 (b) Pledged assets – (FVOCI/available-for-sale)

	2018 KShs'000	2017 KShs'000
Debt securities	1,863,042	4,915,107
	1,863,042	**4,915,107**
Maturity analysis		
Maturing after 6 months but within 12 months	1,863,042	2,336,798
Maturing after 12 months but within 5 years	-	2,578,309
	1,863,042	**4,915,107**

Dated pledged assets at fair value through OCI had a redemption value at 31 December 2018 of KShs 2,000,000,000 (2017: KShs 3,500,000,000).

The weighted average effective interest yield on investment securities at FVOCI on 31 December 2018 was 10.77% (2017:11.34%). A fair value loss of KShs 320,469,000 (2017: Gain of KShs 298,645,000) has been recognised in the statement of other comprehensive income on page 12. A realised gain of KShs 891,000 (2017: KShs 1,580,700) has been transferred to the statement of profit or loss.

These transactions are conducted under terms that are usual and customary to security lending, and security borrowings and lending activities.

Notes (continued)

22.1 Reconciliation of expected credit losses for debt financial investments measured at fair value through OCI:

	Opening ECL 1 January 2018	Total transfers between stages	Income statement movements: ECL on new exposure raised	Income statement movements: Subsequent changes in ECL	Income statement movements: Change in ECL due to derecognition	Net ECL raised/ (released)[1]	Impairment accounts written-off	Closing ECL 31 December 2018
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Financial investments								
Pledged assets at FVOCI	**-**	**-**	**(317)**	**-**	**-**	**(317)**	**-**	**(317)**
Sovereign								
Stage 1	-	-	(317)	-	-	**(317)**	-	**(317)**
Financial investments at FVOCI								
Sovereign	**(2,859)**	**-**	**(1,344)**	**189**	**2,568**	**1,413**	**-**	**(1,446)**
Stage 1	(2,859)	-	(1,344)	189	2,568	**1,413**	-	(1,446)
Total	**(2,859)**	**-**	**(1,661)**	**189**	**2,568**	**1,096**	**-**	**(1,763)**

[1] *Net impairments raised/(released) less recoveries of amounts written off in previous years equals income statement impairment charge (refer credit impairment charges note).*

Reconciliation of fair value through OCI reserve for debt financial investments measured at fair value through OCI

	Balance at beginning of the year	Reclassifications	Net change in fair value	Realised fair value adjustments and reversal to profit or loss	Total fair value movements	Exchange and other movements	Balance at end of the year
	KShs	KShs	KShs	KShs	KShs	KShs	KShs
Financial investments	**(343,317)**	**-**	**320,469**	**891**	**321,360**	**-**	**(21,957)**
Sovereign	(343,317)	-	320,469	891	**321,360**	-	(21,957)

Notes (continued)

23 Financial investments – (amortised cost/held to maturity)

	2018 KShs'000	2017 KShs'000
Pledged assets – (amortised cost/held to maturity)	3,912,057	-
Financial assets – (amortised cost/held to maturity)	19,288,899	5,444,178
	23,200,956	**5,444,178**

a) Pledged assets – (amortised cost/held to maturity)

	2018 KShs'000	2017 KShs'000
Amortised cost debt securities	3,913,271	-
Expected loss	(1,214)	-
	3,912,057	**-**
Maturity analysis		
Maturing after 6 months but within 12 months	2,902,127	-
Maturing after 12 months but within 5 years	1,009,930	-
	3,912,057	**-**

Dated pledged assets at amortized cost had a redemption value at 31 December 2018 of KShs 4,000,000,000 (2017: KShs 1,500,000,000).

These transactions are conducted under terms that are usual and customary to security lending, and security borrowings and lending activities.

b) Financial assets – (amortised cost/held to maturity)

	2018 KShs'000	2017 KShs'000
Debt securities – at fair value:		
Listed	19,305,212	5,444,178
Gross financial investments at amortised cost	**19,305,212**	**5,444,178**
Allowances for impairments		
Expected credit loss for financial investments measured at amortised cost (IFRS 9)	(16,313)	-
Credit impairment allowances	**(16,313)**	**-**
Net financial investments at amortised cost	**19,288,899**	**5,444,178**
Comprising:		
Government bonds	18,843,069	4,684,783
Government treasury bills	445,830	759,395
	19,288,899	**5,444,178**
Maturity analysis:		
Maturing within 1 month	-	-
Maturing after 1 month but within 6 months	3,578,824	-
Maturing after 6 months but within 12 months	509,026	-
Maturing after 12 months but within 5 years	3,543,022	5,444,178
Maturing after 5 years	11,658,027	-
	19,288,899	**5,444,178**

Dated held to maturity assets had a redemption value at 31 December 2018 of KShs 19,069,656,000 (2017: KShs 5,294,138,000).

The weighted average effective interest yield on held to maturity investment securities at 31 December 2018 was 10.31% (2017: 9.14%).

Notes (continued)

23 Financial investments – (amortised cost/held to maturity) (continued)

Reconciliation of expected credit losses for debt financial investments measured at amortised cost

	Opening ECL 1 January 2018	Total transfers between stages	Income statement movements: ECL on new exposure raised	Income statement movements: Subsequent changes in ECL	Income statement movements: Change in ECL due to derecognition	Net ECL raised/ (released)[1]	Impairment accounts written-off	Exchange and other movements	Closing ECL 31 December 2018
BANK	**KSh' 000**	**KSh' 000**	**KSh' 000**	**KSh' 000**	**KSh' 000**	**KSh' 000**	**KSh' 000**	**KSh' 000**	**KSh' 000**
Sovereign	**(245)**	**-**	**(466)**	**64**	**-**	**(402)**	**-**	**-**	**(647)**
Stage 1	(245)	-	(466)	64	-	(402)	-	-	(647)
Financial Investments Amortised cost									
Sovereign	**(11,021)**	**-**	**(10,960)**	**3,946**	**2,358**	**(4,657)**	**-**	**-**	**(15,666)**
Stage 1	(11,010)	-	(10,960)	3,946	2,358	(4,657)	-	-	(15,666)
Stage 2	(11)	-	-	-	-	-	-	-	-
Pledged assets	**(3,725)**	**-**	**2,416**	**94**	**-**	**2,511**	**-**	**-**	**(1,214)**
Stage 1	(537)	-	-	94	-	94	-	-	(443)
Stage 2	(3,188)	-	2,416	-	-	2,416	-	-	(771)
Total	**(14,990)**	**-**	**(9,010)**	**4,104**	**2,358**	**(2,548)**	**-**	**-**	**(17,527)**

[1] *Net impairments raised/(released) less recoveries of amounts written off in previous years equals income statement impairment charge (refer to the credit impairment charges note).*

Notes (continued)

24 Derivative assets and derivative liabilities

All derivatives are classified as held-for-trading.

24.1 Use and measurement of derivative instruments

In the normal course of business, the Bank enters into a variety of derivative transactions for both trading and hedging purposes. Derivative financial instruments are entered into for trading purposes and for hedging foreign exchange, interest rate, inflation and for credit exposures. Derivative instruments used by the Bank in both trading and hedging activities include swaps, options, forwards, futures and other similar types of instruments based on foreign exchange rates, credit risk, inflation risk, interest rates and the prices of equities.

The risks associated with derivative instruments are monitored in the same manner as for the underlying instruments. Risks are also measured across the product range in order to take into account possible correlations.

The fair value of all derivatives is recognised in the statement of financial position and is only netted to the extent that there is both a legal right of set-off and an intention to settle on a net basis, or the intention to realise the derivative asset and settle the derivative liability simultaneously.

Swaps are transactions in which two parties exchange cash flows on a specified notional amount for a predetermined period.

The major types of swap transactions undertaken by the Bank are as follows:

a) Interest rate swap contracts which generally entail the contractual exchange of fixed and floating interest payments in a single currency, based on a notional amount and an interest reference rate.

b) Options are contractual agreements under which the seller grants the purchaser the right, but not the obligation, either to buy (call option) or to sell (put option) by or at a set date, a specified amount of a financial instrument or commodity at a predetermined price. The seller receives a premium from the purchaser for this right. Options may be traded Over The Counter (OTC) or on a regulated exchange.

c) Forwards and futures are contractual obligations to buy or sell financial instruments on a future date at a specified price. Forward contracts are tailor-made agreements that are transacted between counterparties in the OTC market, whereas futures are standardised contracts transacted on regulated exchanges.

24.2 Derivatives held-for-trading

The Bank transacts derivative contracts to address client demand both as a market maker in the wholesale markets and in structuring tailored derivatives for clients. The Bank also takes proprietary positions for its own account. Trading derivative products include the following derivative instruments:

24.2.1 Foreign exchange derivatives

Foreign exchange derivatives are primarily used to economically hedge foreign currency risks on behalf of clients and for the bank's own positions. Foreign exchange derivatives primarily consist of foreign exchange forwards and swaps, foreign exchange futures and foreign exchange options.

24.2.2 Interest rate derivatives

Interest rate derivatives are primarily used to modify the volatility and interest rate characteristics of interest-earning assets and interest-bearing liabilities on behalf of clients and for the Bank's own positions. Interest rate derivatives primarily consist of bond options, caps and floors, forwards, options, swaps and swap options.

Notes (continued)

24 Derivative assets and derivative liabilities (continued)

24.3 Day one profit or loss

Where the fair value of an instrument differs from the transaction price, and the fair value of the instrument is evidenced by comparison with other observable current market transactions in the same instrument, or based on a valuation model whose variables include only data from observable markets, the difference, commonly referred to as day one profit or loss, is recognised in profit or loss immediately. If the fair value of the financial instrument is not able to be evidenced by comparison with other observable current market transactions in the same instrument or non-observable market data is used as part of the input to the valuation models, any resulting difference between the transaction price and the valuation model is deferred and subsequently recognised in accordance with the Bank's accounting policies (refer to accounting policy 2.5 – Financial instruments).

24.4 Fair values

The fair value of a derivative financial instrument represents, for quoted instruments in an active market, the quoted market price and, for an unquoted instrument, the present value of the positive and/or negative cash flows which would have occurred if the rights and obligations arising from that instrument were closed out in an orderly marketplace transaction at the reporting date.

24.5 Notional amount

The contract/notional amount is the sum of the absolute value of all bought and sold contracts. The notional amounts have been translated at the closing exchange rate at the reporting date where cash flows are receivable in foreign currency. The amount cannot be used to assess the market risk associated with the positions held and should be used only as a means of assessing the bank's participation in derivative contracts.

	2018	2018 Fair values		2017	2017 Fair values	
	Notional contract amount KShs'000	Assets KShs'000	Liabilities KShs'000	Notional contract amount KShs'000	Assets KShs'000	Liabilities KShs'000
Foreign exchange derivatives						
Currency forwards	21,217,066	68,719	474,075	17,445,355	185,265	216,441
Currency swaps	41,953,501	434,412	213,484	30,223,913	64,039	451,707
Currency options	16,400,922	263,256	177,888	18,403,411	867,354	183,107
Total over-the-counter derivatives	**79,571,490**	**766,387**	**865,447**	**66,072,679**	**1,116,658**	**851,255**
Interest rate derivatives						
Interest rate swaps	58,532,021	749,079	1,016,211	48,583,192	1,085,227	1,387,092
Cross currency interest rate swaps	-	-	-	4,154,802	189,216	189,216
Total over-the-counter derivatives	**58,532,021**	**749,079**	**1,016,211**	**52,737,994**	**1,274,443**	**1,576,308**
Total derivative assets held for trading	**138,103,511**	**1,515,466**	**1,881,658**	**118,810,673**	**2,391,101**	**2,427,563**
Current	86,671,101	697,359	852,660	78,456,434	894,299	831,596
Non-current	51,432,410	818,107	1,028,998	40,354,239	1,496,802	1,595,967
Total	**138,103,511**	**1,515,466**	**1,881,658**	**118,810,673**	**2,391,101**	**2,427,563**

Notes (continued)

25 Loans and advances to banks

	2018 KShs'000	2017 KShs'000
Balances with banks	6,989,101	8,280,302
Balances due from group companies (Note 43.1)	21,306,058	4,447,484
Gross loans and advances to banks	**28,295,159**	**12,727,786**
Impairment Stages 1 & 2 (performing loans)	(583)	(61,539)
Impairment Stage 3 (non-performing loans)	-	(25,738)
Credit impairment allowances	**(583)**	**(87,277)**
Net loans and advances to banks	**28,294,576**	**12,640,509**
Maturity analysis:		
Redeemable on demand	6,474,332	9,696,108
Maturing within 1 month	21,820,244	2,944,401
Net loans and advances to banks	**28,294,576**	**12,640,509**

Notes (continued)

25.1 Impairment reserve

Reconciliation of expected credit losses for loans and advances to banks measured at amortised cost:

	Opening ECL 1 January 2018	Total transfers between stages	Income statement movements: ECL on new exposure raised	Income statement movements: Change in ECL due to modifications	Income statement movements: Subsequent changes in ECL	Income statement movements: Change in ECL due to derecognition	Net ECL raised/ (released)[1]	Impairment accounts written-off	Exchange and other movements	Closing ECL 31 December 2018
	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000	KShs'000
Bank	**90,380**	**-**	**17**	**-**	**265**	**(81,328)**	**(81,063)**	**-**	**(8,734)**	**583**
Stage 1	61,539	64	10	-	265	(52,551)	**(52,286)**	-	(8,734)	**583**
Stage 2	64	(64)	7	-	-	-	**-**	-	-	**-**
Stage 3	28,777	-	-	-	-	(28,777)	**(28,777)**	-	-	**-**
Total	**90,380**	**-**	**17**	**-**	**265**	**(81,328)**	**(81,063)**	**-**	**(8,734)**	**583**

[1] *Net impairments raised/(released) less recoveries of amounts written off in previous years equals income statement impairment charge (refer credit impairment charges note).*

Year ended 31 December 2017	Specific impairment KShs'000	Portfolio impairment KShs'000	Total KShs'000
At start of year	63,373	330,271	393,644
Amounts written off during the year as uncollectible	(37,635)	-	(37,635)
Amounts recovered during the year	-	(268,732)	(268,732)
At end of year	**25,738**	**61,539**	**87,277**

The 2017 provision arises from exposures held with banks which were placed under statutory management in Kenya and the lack of foreign currency in the South Sudan operating environment.

Notes (continued)

26 Loans and advances to customers

26.1 Net loans and advances

	2018 KShs'000	2017 KShs'000
Mortgage lending	21,024,274	17,975,608
Instalment sales	15,735,947	14,000,974
Overdraft and other demand lending	23,153,478	23,414,144
Term lending	97,330,386	79,833,843
Card lending	610,492	575,246
Gross loans and advances to customers	**157,854,577**	**135,799,815**
Allowances for impairments		
Credit impairments for loans and advances (IAS 39) (note 26.2)	-	(5,264,005)
Expected credit loss for loans and advances measured at amortised cost (IFRS 9) (note 26.2)	(11,250,460)	-
Credit impairment allowances	**(11,250,460)**	**(5,264,005)**
Net loans and advances	**146,604,117**	**130,535,810**
Maturity analysis:		
Redeemable on demand	20,587,811	18,016,245
Maturing within 1 month	10,826,141	11,609,492
Maturing after 1 month but within 6 months	12,646,294	16,938,688
Maturing after 6 months but within 12 months	4,812,204	3,834,190
Maturing after 12 months but within 5 years	46,316,216	40,091,563
Maturing after 5 years	51,415,451	40,045,632
Net loans and advances	**146,604,117**	**130,535,810**

The weighted average effective interest rate on loans and advances to customers as at 31 December 2018 was 10.49% (2017: 10.68%). The Bank extends advances to personal, commercial and corporate sectors as well as to the public sector. Advances made to individuals are mostly in the form of mortgages, instalment sales and overdrafts.

Notes (continued)

26 Loans and advances to customers (continued)

26.2 Net loans and advances

Reconciliation of expected credit losses for loans and advances to customers measured at amortised cost:

A reconciliation of the expected credit loss for loans and advances, by class:

	Opening ECL 1 January 2018	Total transfers between stages	Income statement movements: ECL on new exposure raised	Income statement movements: Subsequent changes in ECL	Income statement movements: Change in ECL due to derecognition	Net ECL raised/ (released)[1]	Impairment accounts written-off	Exchange and other movements	Closing ECL 31 December 2018	Interest in suspense movement	Total
Customers	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Mortgage loans	**653,664**	**-**	**13,418**	**147,392**	**-**	**160,810**	**(12,832)**	**8,947**	**810,589**	**31,316**	**841,906**
Stage 1	15,476	25,087	4,655	(27,804)	-	(23,149)	-	4,255	21,669	-	21,669
Stage 2	178,453	(23,359)	8,763	16,805	-	25,569	-	356	181,018	-	181,018
Stage 3	459,735	(1,728)	-	158,390	-	158,390	(12,832)	4,337	607,902	31,316	639,218
Vehicle and asset finance	**1,259,900**	**-**	**180,186**	**608,622**	**-**	**788,808**	**(473,314)**	**(82,447)**	**1,492,947**	**(19,920)**	**1,473,027**
Stage 1	103,558	5,938	66,365	(65,567)	-	798	-	-	110,294	-	110,294
Stage 2	279,476	(17,542)	113,821	102,850	-	216,672	-	-	478,606	-	478,606
Stage 3	876,866	11,604	-	571,338	-	571,338	(473,314)	(82,447)	904,046	(19,920)	884,127
Card debtors	**53,919**	**-**	**3,827**	**54,114**	**-**	**57,941**	**(50,483)**	**(9,790)**	**51,587**	**-**	**51,587**
Stage 1	14,820	410	2,616	(681)	-	1,935	-	-	17,165	-	17,165
Stage 2	20,891	1,099	1,211	(6,857)	-	(5,646)	-	-	16,345	-	16,345
Stage 3	18,207	(1,509)	-	61,652	-	61,652	(50,483)	(9,790)	18,077	-	18,077
Other loans and advances	**1,726,445**	**-**	**312,410**	**45,279**	**-**	**357,689**	**(262,836)**	**83,990**	**1,905,288**	**123,469**	**2,028,757**
Stage 1	164,191	23,995	96,022	(109,714)	-	(13,692)	-	944	175,437	-	175,437
Stage 2	781,513	(81,386)	216,388	(241,334)	-	(24,946)	-	(529)	674,651	-	674,651
Stage 3	780,741	57,392	-	396,327	-	396,327	(262,836)	83,575	1,055,199	123,469	1,178,668
Corporate	**5,280,395**	**-**	**413,142**	**872,997**	**(322,146)**	**963,993**	**-**	**(52,314)**	**6,192,074**	**663,110**	**6,855,184**
Stage 1	405,041	(71,828)	169,461	58,377	(110,997)	116,842	-	-	450,055	-	450,055
Stage 2	2,103,329	(1,848,316)	41,976	(28,611)	(76,011)	(62,646)	-	(52,314)	140,052	-	140,052
Stage 3	2,772,025	1,920,144	201,705	843,231	(135,139)	909,798	-	-	5,601,967	663,110	6,265,077
Total	**8,974,322**	**-**	**922,984**	**1,728,403**	**(322,146)**	**2,329,241**	**(799,465)**	**(51,614)**	**10,452,484**	**797,976**	**11,250,460**

[1] *Net impairments raised/(released) less recoveries of amounts written off in previous years equals income statement impairment charge (refer credit impairment charges note).*

Notes (continued)

26 Loans and advances to customers (continued)

26.2 Impairment reserve (continued)

Year ended 31 December 2017	Specific impairment KShs'000	Portfolio impairment KShs'000	Total KShs'000
At start of year	**1,653,491**	**1,479,177**	**3,132,668**
Amounts written off during the year as uncollectible	(944,175)	-	**(944,175)**
Amounts recovered during the year (Note 26.3)	(100,406)	-	**(100,406)**
Provision for loans impairment (Note 26.3)	2,634,690	541,228	**3,175,918**
At end of year	**3,243,600**	**2,020,405**	**5,264,005**

26.3 Loans impairment charge

	2018 KShs'000	2017 KShs'000
Loans impairment for financial investments	1,455	-
Loans impairment for non-performing customer loans (Note 26.2)	2,097,504	2,634,690
Loans impairment for performing customer loans (Note 26.2)	231,736	541,228
Loans impairment for performing bank loans (Note 25.2)	(81,063)	-
Loans impairment for non-performing off balance sheet Letters of credit and guarantees(Note 42.2)	19,447	-
Loans impairment for performing off balance sheet Letters of credit and guarantees(Note 42.3)	(53,534)	-
Amounts recovered during the year	(151,083)	(268,732)
Amounts recovered during the year for customer loans (Note 28.2)	-	(100,406)
Recoveries of amounts previously written off	-	(45,455)
Net impairment charge on loans and advances	**2,064,462**	**2,761,325**

The directors are of the opinion that net recoverable amounts are reasonable and are expected to be realised based on past experience.

26.4 Instalment sale and finance leases

The Bank holds instalment sales contracts with customers where the Bank finances the purchase of assets under a series of contracts which transfer title to the Bank as security for the loan. The Bank receives the lease payments and sets off the payments against the principal loan and interest repayments. While in principal the Bank only finances the purchase of the assets, the agreements that are necessary to execute the arrangement confer a lessor status on the Bank.

Notes (continued)

26 Loans and advances to customers (continued)

26.4 Instalment sale and finance leases (continued)

	2018 KShs'000	2017 KShs'000
Gross investment in Instalment sale and finance leases:		
Not later than 1 year	1,048,546	1,285,172
Later than 1 year and not later than 5 years	14,446,703	12,446,683
Later than 5 years	240,698	460,600
	15,735,947	**14,192,455**

The amount of finance lease receivable included above is KShs nil (2017: KShs nil).

Impairment provisions of KShs 672,147,000 (2017: KShs 727,413,000) for instalment sale and finance lease receivables are included in the impairment for non-performing loans.

26.5 Loans and advances to employees

The aggregate amount of loans and advances to employees on the statement of financial position is:

	2018 KShs'000	2017 KShs'000
At start of year	**3,848,482**	**3,708,037**
New loans issued	1,564,065	1,104,356
Interest	437,271	160,805
Loan repayments	(1,655,191)	(1,124,716)
At end of year	**4,194,627**	**3,848,482**

27 Other assets and prepayments

Uncleared effects	1,600,069	1,846,046
Prepayments	491,935	463,381
Off market loan adjustment	686,626	833,640
Due from group companies (Note 43.7)	845,460	414,585
Other receivables	108,104	90,188
	3,732,194	**3,647,840**

The off-market adjustment relates to the prepaid benefit granted to staff, being the difference between the fair value of the staff loans and the initial cash outflow. The fair value of future cash flows are discounted at a market related rate. The asset represents the Bank's right to receive future service from employees.

28 Investment in subsidiaries

	2018 KShs'000	2017 KShs'000
Stanbic Nominees Limited - 100% ownership	2	2
	2	**2**

Notes (continued)

28 Investment in subsidiaries (continued)

Stanbic Nominees Limited was dormant during the two financial years. The Bank's investment in Stanbic Insurance Agency Limited was sold off to Stanbic Holdings Plc in 2017.

The principal place of business for the subsidiary is Stanbic Bank Centre, Chiromo Road.

There were no significant restrictions on the Bank’s ability to access the assets and settle liabilities of the subsidiary. The total amount disclosed as investment in a subsidiary is a non-current asset.

29 Other investments

	2018 KShs’000	2017 KShs’000
Unquoted:		
Equity investment at fair value through profit and loss (default)	17,500	17,500
At 31 December	**17,500**	**17,500**

The investment is in Anglo African Property Holding Limited where the Bank holds a beneficial interest of 1%. The investment is unquoted and its carrying value (cost) is estimated to approximate the fair value.

Notes (continued)

30 Property and equipment

	Land & Premises KShs'000	Equipment Furniture & Fittings KShs'000	Motor Vehicles KShs'000	Work in Progress (WIP) KShs'000	Total KShs'000
31 December 2018					
Opening net book amount	**330,525**	**1,739,877**	**63,501**	**171,516**	**2,305,419**
Additions	-	235,686	8,553	118,364	**362,603**
Transfer from work in progress	-	108,948	-	(108,948)	**-**
Disposals	-	(12,239)	(28,122)	-	**(40,361)**
Depreciation charge on disposal	-	8,440	28,122	-	**36,562**
Translation differences	-	(18,251)	-	-	**(18,251)**
Depreciation charge	(15,666)	(381,715)	(18,032)	-	**(415,413)**
Hyper inflation adjustment	-	3,698	-	-	**3,698**
Closing net book value	**314,859**	**1,684,444**	**54,022**	**180,932**	**2,234,257**
At 31 December 2018					
Cost	473,908	4,053,649	173,777	180,932	**4,882,266**
Accumulated depreciation	(159,049)	(2,369,205)	(119,755)	-	**(2,648,009)**
Net book amount	**314,859**	**1,684,444**	**54,022**	**180,932**	**2,234,257**

	Land & Premises KShs'000	Equipment Furniture & Fittings KShs'000	Motor Vehicles KShs'000	Work in Progress (WIP) KShs'000	Total KShs'000
31 December 2017					
Opening net book amount	**346,191**	**1,780,319**	**26,110**	**105,026**	**2,257,646**
Additions	-	294,077	48,295	114,882	**457,254**
Transfer from work in progress	-	48,392	-	(48,392)	**-**
Disposals	-	(15,357)	(9,694)	-	**(25,051)**
Depreciation charge on disposal	-	9,457	9,694	-	**19,151**
Translation differences	-	(30,175)	-	-	**(30,175)**
Depreciation charge	(15,666)	(352,095)	(10,904)	-	**(378,665)**
Hyper inflation adjustment	-	5,259	-	-	**5,259**
Closing net book value	**330,525**	**1,739,877**	**63,501**	**171,516**	**2,305,419**
At 31 December 2017					
Cost	473,908	3,737,195	193,346	171,516	**4,575,965**
Accumulated depreciation	(143,383)	(1,997,318)	(129,845)	-	**(2,270,546)**
Net book amount	**330,525**	**1,739,877**	**63,501**	**171,516**	**2,305,419**

Work in progress is composed of refurbishments and equipment for branches and projects that had not been completed as at year end. The total amount disclosed as property and equipment is non-current. As at 31 December 2018 and 31 December 2017, there were no items of property and equipment pledged by the Bank to secure liabilities.

Notes (continued)

30 Property and equipment (continued)

Revaluation of land and buildings

The revaluation reserve in equity relates to the value of the Stanbic office in Chiromo at the point of merger between CfC Bank and Stanbic Bank in 2008. The fair value of the properties was determined using the market comparable method. This means that valuations performed by the valuer were based on active market prices, significantly adjusted for differences in the nature, location or condition of the specific property.

As the functional currency of Stanbic Bank South Sudan branch is the currency of a hyperinflationary economy, property, plant and equipment relating to this Branch is restated by applying the change in the general price indices from the date of acquisition to the current reporting date.

Depreciation relating to the property, plant and equipment of Stanbic Bank South Sudan branch is based on the restated amounts, which have been adjusted for the effects of hyperinflation.

Notes (continued)

31 Intangible assets

Year ended 31 December 2018	Work in progress KShs'000	Computer Software KShs'000	Total KShs'000
Cost			
At 1 January	**177,251**	**2,739,505**	**2,916,756**
Additions	134,480	10,206	**144,686**
Translation differences	-	(415)	**(415)**
Effects of Hyperinflation	-	(410)	**(410)**
As at 31 December	**311,731**	**2,748,886**	**3,060,617**
Amortisation			
At 1 January	-	(1,836,242)	**(1,836,242)**
Amortisation for the year	-	(191,804)	**(191,804)**
Translation differences	-	39	**39**
At 31 December	**-**	**(2,028,007)**	**(2,028,007)**
Net Book value At 31 December	**311,731**	**720,879**	**1,032,610**
At 31 December 2018			
Cost	311,731	2,748,886	**3,060,617**
Accumulated amortisation	-	(2,028,007)	**(2,028,007)**
Net book amount	**311,731**	**720,879**	**1,032,610**

Year ended 31 December 2017	Work in progress KShs'000	Computer Software KShs'000	Total KShs'000
Cost			
At 1 January	**101,620**	**2,379,255**	**2,480,875**
Additions	75,631	360,912	**436,543**
Translation differences	-	(900)	**(900)**
Effects of Hyperinflation	-	238	**238**
As at 31 December	**177,251**	**2,739,505**	**2,916,756**
Amortisation			
At 1 January	-	(1,657,662)	**(1,657,662)**
Amortisation for the year	-	(178,580)	**(178,580)**
At 31 December	**-**	**(1,836,242)**	**(1,836,242)**
Net Book value At 31 December	**177,251**	**903,263**	**1,080,514**
At 31 December 2017			
Cost	177,251	2,739,505	**2,916,756**
Accumulated amortisation	-	(1,836,242)	**(1,836,242)**
Net book amount	**177,251**	**903,263**	**1,080,514**

As the functional currency of Stanbic Bank South Sudan branch is the currency of a hyperinflationary economy, intangible assets relating to this branch are hyperinflated by applying the change in the general price indices from the date of acquisition to the current reporting date.

Amortisation relating to intangible assets of Stanbic Bank South Sudan branch is based on the hyperinflated amounts, which have been adjusted for the effects of hyperinflation.

The total amount disclosed as intangible assets is non-current and relates to computer software. Work in progress relates to computer software for upgrades in core banking and the flow credit workflow system had not been completed as at year end.

As at 31 December 2018, the intangible assets had an average remaining useful life of 3 years.

Notes (continued)

32 a) i) Deferred income tax asset

	Note	2018 KShs'000	2017 KShs'000
At start of year		**(2,488,760)**	**(1,475,972)**
Impact of initial application of IFRS 9	2 (c) (ii)	(670,958)	
		(3,159,718)	**(1,475,972)**
Credit /debit to statement of profit or loss	16	(619,232)	(1,014,112)
Previous year deferred income tax over provision	16	606,494	-
Credit/ debit to other comprehensive income	32 (a) (ii)	(33,452)	1,324
At end of year		**(3,205,907)**	**(2,488,760)**

Deferred income tax (assets)/liabilities and deferred income tax (credit)/charge in the income statement and other comprehensive income are attributable to the following items:-

a) ii) Deferred income tax asset

Year ended 31 December 2018	01.01.2018 KShs'000	(Credited)/ charged to statement of profit or loss KShs'000	Credited to OCI KShs'000	31.12.2018 KShs'000
Arising from:				
Property and equipment	106,178	(57,641)	-	**48,537**
Expected credit loss charges	(2,379,210)	(248,937)	-	**(2,628,147)**
Leasing	-	-	-	**-**
Unrealised gain on South Sudan paid up capital	(217,650)	217,650	-	**-**
Unrealised gain on bonds – FVOCI	41,223	-	(33,452)	**7,771**
Unrealised gain on bonds – Held For Trading	(37,114)	(74,104)	-	**(111,218)**
Other provisions	(680,381)	166,751	-	**(513,630)**
Exchange difference on translation	7,236	(7,236)	-	**-**
South Sudan deffered tax asset	-	(9,220)	-	**(9,220)**
Net deferred income tax asset	**(3,159,718)**	**(12,738)**	**(33,452)**	**(3,205,907)**

Year ended 31 December 2017	01.01.2017 KShs'000	(Credited)/ charged to statement of profit or loss KShs'000	Credited to OCI KShs'000	31.12.2017 KShs'000
Arising from:				
Property and equipment	45,596	60,582	-	**106,178**
Expected credit loss charges	(941,498)	(766,754)	-	**(1,708,252)**
Leasing	(21,487)	21,487	-	**-**
Unrealised gain on South Sudan paid up capital	92,004	(309,654)	-	**(217,650)**
Unrealised gain on bonds – Available-For-Sale	53,055	(13,156)	1,324	**41,223**
Unrealised gain on bonds – Held For Trading	172,935	(210,049)	-	**(37,114)**
Other provisions	(873,793)	193,412	-	**(680,381)**
Exchange difference on translation	(2,784)	10,020	-	**7,236**
South Sudan deffered tax asset	-	-	-	**-**
Net deferred income tax asset	**(1,475,972)**	**(1,014,112)**	**1,324**	**(2,488,760)**

Notes (continued)

32 b) Deferred income tax liability

	2018 KShs'000	2017 KShs'000
At start of year	**38,859**	**7,699**
Debit to statement of profit or loss (Note 16)	(38,859)	26,064
Debit to other comprehensive income	-	5,096
At end of year	**-**	**38,859**

The total amount disclosed as deferred income tax liability is a non-current liability.

As the functional currency of Stanbic Bank South Sudan branch is the currency of a hyperinflationary economy, deferred tax relating to this branch is recognised using the liability method, providing for temporary differences arising between the tax bases of assets and liabilities and their restated carrying amounts.

	01.01.2018	(Credited)/ charged to statement of profit or loss	Credited to OCI	31.12.2018
Year ended 31 December 2018	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Arising from:				
Property and equipment	38,859	(38,859)	-	**-**
Net deferred income tax liability	**38,859**	**(38,859)**	**-**	**-**

	01.01.2017	(Credited)/ charged to statement of profit or loss	Credited to OCI	31.12.2017
Year ended 31 December 2017	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Arising from:				
Property and equipment	7,699	26,064	5,096	**38,859**
Net deferred income tax liability	**7,699**	**26,064**	**5,096**	**38,859**

33 Current income tax

The current income tax payable and current income tax receivable have been separately recognised as Kenya and South Sudan have no legal enforceable right to set off current tax.

a) Current income tax (recoverable) /payable	2018 KShs'000	2017 KShs'000
As at 1 January	**-**	**1,384,938**
South sudan tax payable (note 33(b)	(16,667)	
Current tax charge (Note 16)	2,905,059	2,061,861
Income tax paid	(1,519,044)	(3,444,103)
Prior year provision	(244,316)	(2,696)
Exchange difference on translation	(27,830)	-
As at 31 December	**1,097,202**	**-**

The amount above relates to current income tax recoverable in Kenya and is current.

Notes (continued)

33 b) Current income tax payable / (recoverable)

	2018 KShs'000	2017 KShs'000
As at 1 January	**(16,667)**	**(33,964)**
Transfer to tax payable account (note 33 a)	16,667	-
Current tax charge (Note 16)	-	14,601
Prior year-provision	-	2,696
As at 31 December	**-**	**(16,667)**

The amount above relates to current income tax payable in South Sudan and is current.

34 Customer deposits

	2018 KShs'000	2017 KShs'000
Current accounts	120,322,739	106,080,404
Call deposits	9,215,602	7,240,980
Savings accounts	42,651,333	26,317,844
Term deposits	16,404,173	13,006,715
LC acceptances	3,664,166	2,760,020
	192,258,013	**155,405,963**
Maturity analysis:		
Redeemable on demand	172,423,765	113,344,837
Maturing within 1 month	6,278,970	27,396,463
Maturing after 1 month but within 6 months	8,963,597	11,706,367
Maturing after 6 months but within 12 months	3,919,456	2,554,910
Maturing after 12 months	672,225	403,386
	192,258,013	**155,405,963**

Deposit products include current accounts, savings accounts, call deposits and fixed deposits. The weighted average effective interest rate on customer deposits as at 31 December 2018 was 3.43% (2017: 2.57%).

35 Amounts due to other banks

	2018 KShs'000	2017 KShs'000
Deposits from banks	12,438,427	25,687,195
Balances due to group companies (43.2)	15,470,813	13,019,940
	27,909,240	**38,707,135**
Maturity analysis:		
Redeemable on demand	3,488,780	8,528,670
Maturing within 1 month	-	17,247,902
Maturing after 1 month but within 6 months	1,476,287	6,164,691
Maturing after 6 months but within 12 months	444,637	5,189,243
Maturing after 12 months	22,499,536	1,576,629
	27,909,240	**38,707,135**

Included in deposits from banks is a borrowing from a syndicate of banks maturing in one year. Interest on these borrowings is at libor + 1.4%.

Notes (continued)

36 a) Other liabilities

	2018 KShs'000	2017 KShs'000
Accruals	2,279,084	1,828,314
Deferred bonus scheme (Note 36(b))	157,791	310,117
Unpresented bank drafts	104,498	111,271
Margin on guarantees and letters of credit	1,331,651	1,520,838
Items in transit	127,585	152,955
Due to group companies (Note 43.8)	257,609	463,369
Sundry creditors	1,382,808	1,038,426
Expected credit losses on off balance sheet items (note 42.3)	138,076	-
	5,779,102	**5,425,290**

Sundry creditors relate to credits in transit, PAYE and VAT payables.

b) Deferred bonus scheme (DBS)

It is essential for the Bank to retain key skills over the longer term. This is done particularly through share-based incentive plans. The purpose of these plans is to align the interests of the Bank, its subsidiaries and employees, as well as to attract and retain skilled, competent people.

The Bank has implemented a scheme to defer a portion of incentive bonuses over a minimum threshold for key management and executives. This improves the alignment of shareholder and management interests by creating a closer linkage between risk and reward, and also facilitates retention of key employees.

All employees granted an annual performance award over a threshold have part of their award deferred. The award is indexed to Standard Bank Group's (SBG) share price and accrues notional dividends during the vesting period, which are payable on vesting. The awards vest in three equal amounts at 18 months, 30 months and 42 months from the date of award. The final pay-out is determined with reference to SBG's share price on vesting date.

The provision in respect of liabilities under the scheme amounts to KShs 157,791,000 at 31 December 2018 (2017: KShs 310,117,000) and the amount charged for the year was KShs 33,501,000 (2017: KShs 257,987,000).

	Units	
Reconciliation	**2018**	**2017**
Units outstanding at beginning of the year	**140,662**	**133,976**
Granted	-	-
Exercised	(80,649)	(116,975)
Lapsed	(13,450)	(15,856)
Transfers	5,675	139,517
Units outstanding at end of the year	**52,238**	**140,662**
Weighted average fair value at grant date (ZAR)*	220.97	155.95
Expected life (years)	2.51	2.51
Risk-free interest rate (%)	-	5.54

** South African Rand*

Notes (continued)

37 Borrowings

At 31 December 2018

	Notional value KShs'000	Carrying value KShs'000	Interest Rate	Date of Issue	Maturity date
CfC Stanbic Bond	4,000,000	3,992,347	12.95%	15-Dec-14	15-Dec-21
Subordinated debt	3,052,017	3,071,666	6.82%	28-Feb-18	28-Feb-28
Total	**7,052,017**	**7,064,013**			

At 31 December 2017

	Notional value KShs'000	Carrying value KShs'000	Interest Rate	Date of Issue	Maturity date
CfC Stanbic Bond	4,000,000	3,989,243	12.95%	15-Dec-14	15-Dec-21
Total	**4,000,000**	**3,989,243**			

There were no charges placed on any of the Bank's assets in relation to these borrowings.

The difference between the carrying and notional value represents, accrued interest and the unamortised issue costs.

Interest expense incurred in the above borrowings was KShs 682,725,000 (2017: KShs 521,104,000). The weighted average effective interest rate on borrowings as at 31 December 2018 was 9.88% (2017: 12.95%).

The surbodinated debt relates to USD 30m obtained from the Standard Bank of South Africa in 2018. There are no covenants relating to this financing.

38 Share capital

Authorised share capital	**2018** Number of Shares (thousands)	Share Capital KShs '000	**2017** Number of Shares (thousands)	Share Capital KShs '000
Authorised share capital of Kshs 20 each	187,250	3,745,000	187,250	3,745,000
And 31 December	**187,250**	**3,745,000**	**187,250**	**3,745,000**

Issued share capital	**2018** Number of Shares (thousands)	Share Capital KShs '000	**2017** Number of Shares (thousands)	Share Capital KShs '000
Balance as at 01 January	170,577	3,411,549	170,577	3,411,549
And 31 December	**170,577**	**3,411,549**	**170,577**	**3,411,549**
Unissued shares	**16,673**	**333,451**	**16,673**	**333,451**

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

Notes (continued)

39 Share premium

	2018 KShs'000	2017 KShs'000
At 01 January	3,444,639	3,444,639
At 31 December	**3,444,639**	**3,444,639**

40 Nature and purpose of reserves

40.1 Revaluation reserve on available-for-sale financial assets/FVOCI

The fair value reserve comprises the cumulative net change in the fair value of available-for-sale/FVOCI financial assets until the investment is derecognised or impaired. The reserve is non-distributable.

40.2 Revaluation reserve on buildings

The revaluation reserve represents solely the surplus on the revaluation of buildings and freehold land net of deferred income tax and is non-distributable. This reserve arose from the merger between CfC Bank Limited and Stanbic Bank Limited in 2008.

40.3 Foreign currency translation reserve

Currency translation reserve comprises all the foreign exchange differences arising from the translation of the financial results of foreign operations.

40.4 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.

Notes (continued)

41 Share-based payment reserve

	2018 KShs'000	2017 KShs'000
At start of year	**16,004**	**13,858**
Equity growth scheme for the year	18,801	2,146
At end of year	**34,805**	**16,004**

The Bank's share incentive scheme enables key management personnel and senior employees of the Bank to benefit from the performance of Standard Bank Group (SBG) shares.

The Bank has two equity-settled schemes, namely the Group Share Incentive Scheme and the Equity Growth Scheme. The Group Share Incentive Scheme confers rights to employees to acquire ordinary shares at the value of the SBG share price at the date the option is granted. The Equity Growth Scheme represents appreciation rights allocated to employees. The eventual value of the right is effectively settled by the issue of shares equivalent in value to the value of the rights. The share appreciation rights granted during the year were valued using Black Scholes pricing model. Each grant was valued separately.

At 31 December 2018, the total amount included in staff costs for Group Share Incentive Scheme was KShs 10,247,000 (2017: KShs 6,085,000) and for Equity Growth Scheme was KShs 8,553,000 (2017: KShs 3,941,000).

The two schemes have five different sub-types of vesting categories as illustrated by the table below:

	Year	% vesting	Expiry
Type A	3, 4, 5	50, 75, 100	10 Years
Type B	5, 6, 7	50, 75, 100	10 Years
Type C	2, 3, 4	50, 75, 100	10 Years
Type D	2, 3, 4	33, 67, 100	10 Years
Type E	3, 4, 5	33, 67, 100	10 Years

A reconciliation of the movement of share options and appreciation rights is detailed below:

	Option price range (ZAR)	Number of options	
Group Share Incentive Scheme	**2018**	**2018**	**2017**
Options outstanding at beginning of the year		**72,251**	**117,563**
Transfers		-	34,126
Exercised	98.80-111.94	(12,251)	(74,750)
Lapsed		-	(4,688)
Options outstanding at end of the year		**60,000**	**72,251**

The weighted average SBG share price for the year to 31 December 2018 was ZAR 192.35 (2017: ZAR 157.29).

The following options granted to employees had not been exercised at 31 December 2018:

Number of ordinary shares	Option price range (ZAR)	Weighted average price (ZAR)	Option expiry period
3,750	111.94	111.94	Year to 31 December 2020
56,250	98.80 - 107.55	101.65	Year to 31 December 2021
60,000			

Notes (continued)
41 Share-based payment reserve (continued)

The following options granted to employees had not been exercised at 31 December 2017:

Number of ordinary shares	Option price range (ZAR)	Weighted average price (ZAR)	Option expiry period
10,750	111.94	111.94	Year to 31 December 2020
61,501	98.80 - 107.55	101.65	Year to 31 December 2021
72,251			

Equity Growth Scheme	Appreciation right price range (ZAR) 2018	Number of rights 2018	Number of rights 2017
Rights outstanding at beginning of the year		**41,813**	**21,375**
Transfers		-	26,013
Exercised	98.80-111.94	(38,813)	-
Lapsed		-	(5,575)
Rights outstanding at end of the year[1]		**3,000**	**41,813**

[1] At 31 December 2018 the Bank would need to issue 1,378 (2017: 39,065) SBG shares to settle the outstanding appreciated rights value.

The following rights granted to employees had not been exercised at 31 December 2018:

Number of rights	Option price range (ZAR)	Weighted average price (ZAR)	Option expiry period
3,000	96.68	96.68	Year to 31 December 2021
3,000			

The following rights granted to employees had not been exercised at 31 December 2017:

Number of rights	Option price range (ZAR)	Weighted average price (ZAR)	Option expiry period
1,375	62.39	62.39	Year to 31 December 2019
16,250	105.60 - 111.94	111.45	Year to 31 December 2020
24,188	98.80 - 96.68	98.54	Year to 31 December 2021
41,813			

Notes (continued)

42 Contingent liabilities

Commitments were with respect to:	2018 KShs'000	2017 KShs'000
Letters of credit and acceptances	3,603,396	4,841,591
Guarantees	75,056,875	34,270,551
Unutilised facilities	10,651,153	6,252,527
	89,311,424	**45,364,669**

42.1 Nature of contingent liabilities

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

Guarantees are generally written by 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 customers' default.

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

A contingent liability exists on an advance payment guarantee.The guarantee was issued on behalf of a well-rated Foreign Bank and a claim has arisen following a disagreement between the applicant (client of the Foreign Bank) and the beneficiary. Whilst the Directors believe that their legal defence is strong, they have been engaging the various stakeholders to this disagreement, in an effort to have the matter resolved amicably. These efforts are progressing well and there is a high likelihood the matter shall be resolved in 2019. The potential amount of payments that the Bank could be required to make if there was an adverse decision is estimated to be up to USD 14.6 million. As at 31 December 2018, the Bank had provided for legal fees of USD 1.5 million, in respect to this matter and does not believe any further provision is required at this stage. The position shall continually be assessed.

42.2 Segmental analysis of off-balance sheet liabilities

	2018		2017	
	KShs'000	%	KShs'000	%
Agriculture	800,681	1%	1,959,763	4%
Manufacturing	7,329,823	8%	3,226,186	7%
Construction	12,939,274	14%	3,806,467	8%
Energy	622,164	1%	8,296,149	18%
Transport and communication	2,002,709	2%	2,832,456	6%
Distribution/wholesale	10,663,335	12%	3,857,709	9%
Financial services	53,322,058	60%	18,103,741	40%
Tourism	169,858	0%	1,111,650	2%
Other activities and social service	1,461,523	2%	2,170,548	5%
	89,311,424	**100%**	**45,364,669**	**100%**

Notes (continued)

42 Contingent liabilities (cont)

42.3 Expected credit losses on off balance sheet items (note 42.2)

	Opening ECL 1 January 2018	Total transfers between stages	Income statement movements: ECL on new exposure raised	Income statement movements: Change in ECL due to modifications	Income statement movements: Subsequent changes in ECL	Net ECL raised/ (released)[1]	Impairment accounts written-off	Exchange and other movements	Closing ECL 31 December 2018
Off balance sheet	**KShs**	**KShs**	**KShs**	**KShs**	**KShs**	**KShs**	**KShs**	**KShs**	**KShs**
Stage 1	**78,848**	**(4,494)**	**36,253**	**-**	**(69,842)**	**(33,589)**	**-**	**-**	**40,765**
Letters of credit	35,953	(4,494)	4,925	-	(30,746)	**(25,821)**	-	-	5,638
Guarantees	42,895	-	31,328	-	(39,096)	**(7,768)**	-	-	35,127
Stage 2	**32,793**	**4,494**	**8,167**	**-**	**(28,112)**	**(19,945)**	**-**	**-**	**17,342**
Letters of credit	18,493	4,494	175	-	(13,999)	**(13,824)**	-	-	9,163
Guarantees	14,300	-	7,992	-	(14,113)	**(6,121)**	-	-	8,179
Stage 3	**60,699**	**-**	**80,146**	**-**	**(60,699)**	**19,447**	**-**	**(177)**	**79,969**
Letters of credit	-	-	80,146	-	(60,699)	**19,447**	-	(177)	19,270
Guarantees	60,699	-	-	-	-	**-**	-	-	60,699
Total ECL	**172,340**	**-**	**124,566**	**-**	**(158,653)**	**(34,087)**	**-**	**(177)**	**138,076**

42.4 Legal proceedings

In the conduct of its ordinary course of business, the Bank is exposed to various actual and potential claims, lawsuits and other proceedings relating to alleged errors and omissions, or non-compliance with laws and regulations. The directors are satisfied, based on present information and the assessed probability of claims arising, that the Bank has adequate insurance programmes and provisions in place to meet such claims. The amounts provided for in other liabilities are KShs 25,000,000 (2017: KShs 25,000,000).

Notes (continued)

43 Related party transactions

The Bank is a wholly owned subsidiary of Stanbic Holdings Plc, which is in turn a subsidiary of Stanbic Africa Holdings Limited (SAHL), incorporated in South Africa. The ultimate parent of the Bank is Standard Bank Group Limited, which is incorporated in the United Kingdom.

There are other companies which are related to Stanbic Bank Kenya Limited through common shareholdings or common directorships.

In the normal course of business, nostro and vostro accounts are operated and placements of both foreign and local currencies are made with the parent company and other group companies at interest rates in line with the market. Outstanding balances at the year-end are unsecured. There have been no guarantees provided or received for any related party balances.

For the year ended 31 December 2018, the Bank has made provision for doubtful debts relating to long outstanding amounts owed by related parties KShs 275,290,000 (2017: KShs 275,290,000) as indicated on Note 43.6.

The relevant balances are as shown below:

43.1 Loans and advances to group banks

	2018 KShs'000	2017 KShs'000
Stanbic Bank Uganda Limited	60,973	19,221
Stanbic Bank Tanzania Limited	1,233	48,733
Standard Bank (Mauritius) Limited	5	27
Standard Bank of South Africa Limited	1,195,452	1,799,470
Standard Bank Isle of Man	20,048,115	2,580,033
Stanbic Bank Botswana Limited	239	-
Stanbic Bank Ghana Limited	41	-
	21,306,058	**4,447,484**
Interest income earned on the above is:	**230,142**	**116,316**

43.2 Deposits due to group to banks

	2018 KShs'000	2017 KShs'000
Standard Bank of South Africa Limited	2,040,969	403,871
Standard Bank Namibia Limited	561	526
Stanbic Bank Uganda Limited	69,597	393,971
Stanbic Bank Zambia Limited	325	366
Stanbic Bank Zimbabwe Limited	814	358
Stanbic Bank Botswana Limited	-	1,350
Standard Bank (Mauritius) Limited	833,845	1,672,616
Stanbic Bank Malawi Limited	582	1,315
Standard Bank Isle of Man	12,513,772	10,542,423
Stanbic Bank Tanzania Limited	10,274	3,096
Standard Bank Swaziland Limited	74	48
	15,470,813	**13,019,940**
Interest expense incurred on the above is:	**737,797**	**237,889**

The weighted average effective interest rate on loans and advances to group companies as at 31 December 2018 is 2.33% (2017: 3.80%) and on amounts due to group companies was 4.41% (2017: 3.13%).

Notes (continued)
43 Related party transactions (continued)

43.3 Deposits due to group companies non-bank

	2018 KShs'000	2017 KShs'000
Stanbic Holdings Plc	150,353	119,490
SBG Securities Limited	286,636	10,693
The Heritage Insurance Company Limited	306,843	479,109
STANLIB Kenya Limited	185,788	150,296
Liberty Life Assurance Kenya Ltd	97,519	110,851
Stanbic Insurance Agency Limited	236,350	39,680
	1,263,489	**910,119**
Interest expense incurred on the above is:	**46,071**	**4,529**

43.4 Trading liabilities with group companies non-ban

SBG Securities Limited	337,287	10,693
STANLIB Kenya Limited	1,295,481	150,296
	1,632,768	**160,989**

43.5 Due to subsidiary

Stanbic Nominees Limited	2	2
	2	**2**

43.6 Key management compensation

Key management personnel include the members of the Stanbic Bank Kenya Limited board of directors and prescribed officers effective for 2018 and 2017. Non-executive directors are included in the definition of key management personnel as required by IAS 24 Related Party Disclosures. The definition of key management includes the close family members of key management personnel and any entity over which key management exercise control or joint control. Close members of family are those family members who may be expected to influence, or be influenced by that person in their dealings with the bank. They include the person's domestic partner and children, the children of the person's domestic partner, and dependants of the person or the person's domestic partner.

Key management have transacted with the Bank as indicated in note 43.6.1 and 43.6.2.

43.6.1 Loans and advances to key management

The aggregate amount of loans to directors, affiliates and their families on the statement of financial position is Kshs 776,515,000 (2017: Kshs 588,641,000).

Loans include mortgage loans, instalment sale and finance leases and credit cards. No specific credit impairments have been recognised in respect of loans granted to key management (2017: KShs nil). The mortgage loans and instalment sale and finance leases are secured by the underlying assets. All other loans are unsecured.

Notes (continued)
43 Related party transactions (continued)

43.6.2 Key management remuneration

	2018 KShs'000	2017 KShs'000
Fees for services as a director	31,633	24,970
Salaries and other short term employment benefits	56,001	87,972
Post-employment pension	3,315	3,036
Share-based payments	6,242	15,864
	97,191	**131,842**

43.7 Other receivable from related companies

	2018	2017
SBG Securities Limited	49,821	38,269
Liberty Life Assurance Kenya Ltd	2,483	172
The Heritage Insurance Company Limited	142	-
Stanbic Holdings Plc	4,779	8,675
Stanbic Bank Uganda Limited	3,645	12,177
Stanbic Bank Tanzania Limited	297,314	297,735
Standard Bank of South Africa Limited	647,186	265,678
Stanbic Bank Zambia Limited	2,275	-
Stanbic Bank Malawi Limited	1,384	3,199
Standard Bank Swaziland Limited	216	-
Standard Bank RDC s.a.r.l	-	655
Standard Bank de Angola S.A.	7,147	27,040
Stanbic Insurance Agency Limited	96,909	31,385
Standard Advisory London Limited	1,619	-
Standard Bank Jersey Limited	1,936	3,017
Standard Bank Isle of Man Limited	-	1,873
STANLIB Kenya Limited	3,525	-
Standard Bank Namibia Limited	367	-
	1,120,750	**689,875**
Provisions on regional costs balances	(275,290)	(275,290)
	845,460	**414,585**
Movement analysis		
At 1 January	**689,875**	**1,075,279**
Additions	1,370,313	644,712
Receipts	(939,438)	(1,030,116)
Closing Balance	**1,120,750**	**689,875**
Provisions on regional costs balances	(275,290)	(275,290)
At 31 December	**845,460**	**414,585**

Notes (continued)
43 Related party transactions (continued)

43.8 Other payables due to related companies

	2018 KShs'000	2017 KShs'000
Standard Bank Malawi Limited	-	1,353
Standard Bank of South Africa Limited	245,592	458,654
Stanbic Bank Uganda Limited	5,697	2,384
Stanbic Bank Tanzania Limited	1,631	816
Standard Bank Jersey Limited	3,167	162
SBG Securities Limited	1,522	-
	257,609	**463,369**
Interest expense incurred on the above is:	**-**	**-**

43.9 Related party expenses

The Bank incurred the following related party expenses payable to the Standard Bank of South Africa:

	2018 KShs'000	2017 KShs'000
Franchise fees	639,799	551,226
Information technology	52,547	93,963
Other operating costs	77,497	67,326
	769,843	**712,515**

44 Notes to the cash flow statement

44.1 Cash flows from operating activities

	2018 KShs'000	2017 KShs'000
Reconciliation of profit before income tax to cash flow from operating activities:		
Net income before income tax	8,785,218	5,412,950
Adjusted for:		
- Amortisation of intangible assets (Note 31)	191,804	178,546
- Depreciation - property and equipment (Note 30)	415,413	377,863
- Other investments	-	(17,500)
- Change in fair value of derivatives	329,730	(552,411)
- Share based payment expense (Note 41)	18,801	2,143
- (Gain)/ Loss on disposal of property and equipment	(3,946)	3,339
- Gain on sale of subsidiary (Note 28)	-	(42,164)
Cash flow from operating activities	**9,737,020**	**5,362,766**

Notes (continued)

44.2 Analysis of cash and cash equivalents

	2018 KShs'000	2017 KShs'000
Cash and balances with CBK	13,044,773	3,704,261
Treasury bills	24,630,105	14,852,344
Loans and advances to banks	26,843,216	9,440,073
Amounts due to other banks	(3,563,714)	(2,200,311)
Cash and cash equivalents at year end	**60,954,380**	**25,796,368**

For the purpose of presentation of cash flows in the financial statements, the cash and cash equivalents include balances with Central Bank of Kenya net of cash reserve ratio, net of balances from banking institutions and treasury bills with a maturity period of three months or less from the contract date.

45 Capital commitments

Capital commitments for the acquisition of property and equipment are summarised below:

	2018 KShs'000	2017 KShs'000
Authorised and contracted for	330,808	237,506
Authorised but not contracted for	1,186,830	704,750

46 Operating leases

The Bank has entered into a number of commercial leases for it premises and office equipment. These leases have an average life of between six years with a renewal option included in the contracts. There are no restrictions placed upon the lessee by entering into these leases such as those concerning dividends or additional debt.

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

	2018 KShs'000	2017 KShs'000
Less than one year	273,999	260,421
Between one and five years	845,488	788,827
More than five years	99,568	9,852
	1,219,055	**1,059,100**

47 Fiduciary activities

The assets held on behalf of individuals, trusts, retirement benefit plans and other institutions:

	2018 KShs'000	2017 KShs'000
Assets held on behalf of individual's trusts and other institutions	**292,161,154**	**266,101,243**

48 Comparatives

Where necessary, comparative figures within notes have been adjusted to either conform to changes in presentation in the current year or for the adoption of new IFRS requirements.