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DIRECTORS AND STATUTORY INFORMATION

FOR THE YEAR ENDED 31 DECEMBER 2011

DIRECTORS

Mr. P.W. Muthoka	Chairman
Dr. M.L. Oduor-Otieno	Chief Executive Officer
Mr. S. Kimani	Retired on 31st May 2011
Mr. J. I. Adongo	
Mr. J.K. Kinyua	
Mrs. C.N. Kimura	Retired on 6th May 2011
Eng. J.M. Ndetto	
Mrs. S.N. Omanga	
Mr. S.N. Shah	
Prof. P.K. Kimuyu	
Mrs. C. Kola	
Mr. Ngeny Biwott	Appointed on 6th May 2011
Mr. J. N. Oigara	Appointed on 12th January 2012

SECRETARY

Mr K.D. Malakwen
PO Box 48400 - 00100
Nairobi, Kenya

AUDITORS

KPMG Kenya, 16th Floor, Lonrho House
Standard Street
PO Box 40612- 00100
Nairobi, Kenya

REGISTERED OFFICES AND PRINCIPAL PLACES OF BUSINESS

Kenya Commercial Bank Limited

Kencom House
Moi Avenue
PO Box 48400- 00100
Nairobi, Kenya

KCB (Tanzania) Limited

Harambee Plaza
Ali Hassan Mwinyi Road/
Kaunda Road Junction
PO Box 804
Dar es Salaam, Tanzania

KCB Sudan Limited

KCB Plaza
Ministry Road
PO Box 47
Juba, Southern Sudan

KCB Bank Uganda Limited

Commercial Plaza
7 Kampala Road
PO Box 7399
Kampala, Uganda

KCB Rwanda SA

Avenue de la Paix
P.O Box 5620
Kigali, Rwanda

SOLICITORS

Various. A list is available at the Bank

REPORT OF THE DIRECTORS

FOR THE YEAR ENDED 31 DECEMBER 2011

The directors submit their report together with the audited financial statements for the year ended 31 December 2011, in accordance with Section 22 of the Banking Act and Section 157 of the Kenyan Companies Act which disclose the state of affairs of Kenya Commercial Bank Limited (the "Bank") and its subsidiaries (collectively referred to as the "Group").

1. Principal activities

The Bank continues to offer corporate and retail banking services. The activities of the subsidiary companies are those set out in note 28 to the financial statements.

2. Results

The results of the Group and the Bank are set out on pages 63 and 65, respectively.

3. Dividend

The directors recommend the payment of a dividend of KShs. 5,492,180,389 which represents KShs. 1.85 per share in respect of the year ended 31 December 2011 (2010: KShs 3,687,824,773 representing KShs. 1.25 per share).

4. Directors

The directors who served during the year and up to the date of this report are set out on page 59.

All directors are non-executive other than the Chief Executive Officer and the Chief Finance Officer.

5. Reserves

The reserves of the Group and Bank are set out on page 69 and page 70 respectively and note 35 on page 117 .

6. Auditors

The auditors, KPMG Kenya, were appointed during the year in place of Ernst & Young and have indicated their willingness to continue in office in accordance with Section 159(2) of the Kenyan Companies Act and subject to Section 24(1) of the Banking Act.

BY ORDER OF THE BOARD



Mr. K.D. Malakwen

SECRETARY

Date: 1st March 2012

STATEMENT OF DIRECTORS' RESPONSIBILITIES

FOR THE YEAR ENDED 31 DECEMBER 2011

The directors are responsible for the preparation and presentation of the financial statements of Kenya Commercial Bank Limited and its subsidiaries set out on pages 63 to 121 which comprise the statements of financial position of the Group and the Bank at 31 December 2011, and the Group and Bank statements of comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

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

Under the Kenyan Companies Act the Directors are required to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Group and of the Bank as at the end of the financial year and of the operating results of the Group for that year. It also requires the directors to ensure the Group keeps proper accounting records which disclose with reasonable accuracy the financial position of the Group and the Bank.

The Directors accept responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgments and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act.

The Directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the Group and the Bank and of the Group operating results.

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

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

Approval of the financial statements

The financial statements, as indicated above, were approved by the Board of Directors on 1st March 2012 and were signed on its behalf by:



Chairman



Chief Executive



Director



Secretary

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF KENYA COMMERCIAL BANK LIMITED

Report on the financial statements

We have audited the consolidated financial statements of Kenya Commercial Bank Limited set out on pages 63 to 121. These financial statements comprise Group's and the Bank's statements of financial position at 31 December 2011 and the statements of comprehensive income, the Group's statements of changes in equity and statements of cash flow for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

As stated on page 61, the Bank's Directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and in the manner required by the Companies Act of Kenya, and for such internal control as the Directors determine necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Group and the Bank at 31 December 2011, and the Group and the Bank's financial performance and the Group and the Bank's cash flows for the year then ended in accordance with International Financial Reporting Standards and the Kenyan Companies Act.

Report on other legal requirements

The Kenyan Companies Act requires us to expressly report to you, based on our audit, that:

1. We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purpose of our audit;
2. In our opinion, proper books of account have been kept by the Bank, so far as appears from our examination of those books; and
3. The Bank's statement of financial position, income statement and statement of comprehensive income are in agreement with the books of account.

KPMG Kenya

Date: 1st March 2012

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	2011 KShs'000	2010 KShs'000
Interest income	8	27,902,652	23,109,793
Interest expense	8	(4,616,241)	(3,464,468)
Net interest income		23,286,411	19,645,325
Fees and commission income		9,184,839	6,788,580
Fees and commission expense		(455,392)	(306,155)
Net fees and commission income		8,729,447	6,482,425
Foreign exchange income	9	3,607,836	2,775,494
Dividend income	10	26,157	1,185
Other operating income	11	854,794	424,379
Operating income		36,504,645	29,328,808
Net impairment on financial assets	12	452,957	(1,117,896)
Other operating expenses	13	(21,828,228)	(18,412,941)
Profit before tax		15,129,374	9,797,971
Income tax expense	14(a)	(4,148,328)	(2,619,998)
Profit for the year		10,981,046	7,177,973
Attributable to:			
Owners of the parent		10,981,046	7,177,973
Non controlling interest		-	-
		10,981,046	7,177,973
Diluted earnings per share (KShs.)	15	3.72	2.76
Dividends per share (KShs.)	16	1.85	1.25

The notes set out on pages 73 to 121 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2011

	2011 KShs'000	2010 KShs'000
Profit for the year	10,981,046	7,177,973
Other comprehensive income		
Exchange differences on translation of foreign operations	(193,666)	(278,084)
Available for sale financial assets:		
-Unrealized gain arising from measurement at fair value	(2,208,502)	14,558
-Cumulative realized gain arising from disposal made during the year	-	(137,110)
Other comprehensive income for the year, net of taxes	(2,402,168)	(400,636)
Total comprehensive income for the year	8,578,878	6,777,337
Attributable to:		
Owners of parent	8,578,878	6,777,337
Non-controlling interest	-	-
	8,578,878	6,777,337

The notes set out on pages 73 to 121 form an integral part of these financial statements.

INCOME STATEMENT OF THE BANK

FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	2011 KShs'000	2010 KShs'000
Interest income	8	25,181,308	21,441,262
Interest expense	8	(3,904,546)	(2,942,881)
Net interest income		21,276,762	18,498,381
Fees and commission income		6,975,620	5,618,346
Fees and commission expense		(438,443)	(306,155)
Net fees and commission income		6,537,177	5,312,191
Foreign exchange income	9	1,940,587	1,357,658
Dividend income	10	26,157	1,519,248
Other operating income	11	803,636	369,830
Operating income		30,584,319	27,057,308
Net impairment on financial assets	12	876,629	(875,411)
Other operating expenses	13	(17,379,082)	(14,644,364)
Profit before tax		14,081,866	11,537,533
Income tax expense	14(a)	(4,243,529)	(2,718,673)
Profit for the year		9,838,337	8,818,860
Diluted earnings per share (KShs.)	15	3.33	3.40
Dividends per share (KShs.)	16	1.85	1.25

The notes set out on pages 73 to 121 form an integral part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME OF THE BANK

FOR THE YEAR ENDED 31 DECEMBER 2011

	2011 KShs'000	2010 KShs'000
Profit for the year	9,838,337	8,818,860
Other comprehensive income		
Available for sale financial assets		
- Unrealized gain arising from measurement at fair value	(2,208,502)	14,558
- Cumulative realized gain arising from disposal made during the year	-	(137,110)
Other comprehensive income for the year, net of taxes	(2,208,502)	(122,552)
Total comprehensive income for the year	7,629,835	8,696,308

The notes set out on pages 73 to 121 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2011

	Note	2011 KShs'000	2010 KShs'000
ASSETS			
Cash and balances with Central Banks	17	42,708,016	26,997,823
Due from banks	18	25,812,084	10,211,008
Held for trading investments	19	367,938	847,876
Available-for-sale investments	20	9,204,501	5,862,488
Loans and advances to customers	21	198,724,919	148,113,364
Held to maturity investments	22	36,432,197	43,398,134
Other assets	23	6,708,391	5,002,289
Tax recoverable	14(b)	20,557	11,009
Deferred tax asset	24	1,055,476	1,126,284
Intangible assets	25	1,516,684	1,368,385
Property and equipment	26(a)	8,017,595	8,271,647
Prepaid operating lease rentals	27	147,801	145,893
TOTAL ASSETS		330,716,159	251,356,200
LIABILITIES			
Due to banks	29	14,105,149	11,056,967
Customer deposits	30	259,308,849	196,974,651
Other liabilities	31	4,292,762	2,356,968
Tax payable	14(b)	119,372	1,837,722
Deferred tax liability	24	-	121
Long term debt	33	8,525,000	-
TOTAL LIABILITIES		286,351,132	212,226,429
EQUITY			
Share capital	34	2,968,746	2,950,260
Reserves	35	35,904,101	32,491,686
Proposed dividend		5,492,180	3,687,825
TOTAL EQUITY		44,365,027	39,129,771
TOTAL LIABILITIES AND EQUITY		330,716,159	251,356,200

The financial statements were approved by the Board of Directors on 1st March 2012 and were signed on its behalf by:



P. W. MUTHOKA
Chairman



DR. M. L. ODUOR-OTIENO
Chief Executive



ENG. J. M. NDETO
Director



K. D. MALAKWEN
Secretary

The notes set out on pages 73 to 121 form an integral part of these financial statements.

STATEMENT OF FINANCIAL POSITION OF THE BANK

AS AT 31 DECEMBER 2011

	Note	2011 KShs'000	2010 KShs'000
ASSETS			
Cash and balances with Central Bank of Kenya	17	20,138,633	13,796,511
Due from banks	18	17,648,880	3,959,963
Held for trading investments	19	367,938	847,876
Available for sale investments	20	9,204,501	5,862,488
Loans and advances to customers	21	179,843,987	137,344,568
Held to maturity investments	22	34,023,362	42,051,335
Other assets	23	4,781,799	4,185,781
Tax recoverable	14(b)	9,418	-
Deferred tax asset	24	606,328	855,115
Intangible assets	25	1,476,594	1,319,367
Property and equipment	26(b)	5,624,766	5,888,285
Prepaid operating lease rentals	27	142,818	143,644
Investment in subsidiaries and associated companies	28	8,624,529	6,769,623
TOTAL ASSETS		282,493,553	223,024,556
LIABILITIES			
Due to banks	29	11,502,571	10,807,301
Customer deposits	30	210,173,514	163,188,681
Other liabilities	31	1,610,203	1,763,732
Tax payable	14(b)	-	1,750,345
Balances due to group companies	32	5,519,607	4,638,052
Long term debt	33	8,525,000	-
TOTAL LIABILITIES		237,330,895	182,148,111
EQUITY			
Share capital	34	2,968,746	2,950,260
Reserves	35	36,701,732	34,238,360
Proposed dividend		5,492,180	3,687,825
TOTAL EQUITY		45,162,658	40,876,445
TOTAL LIABILITIES AND EQUITY		282,493,553	223,024,556

The financial statements were approved by the Board of Directors on 1st March 2012 and were signed on its behalf by:



P. W. MUTHOKA
Chairman



DR. M. L. ODUOR-OTIENO
Chief Executive



ENG. J. M. NDETO
Director



K. D. MALAKWEN
Secretary

The notes set out on pages 73 to 121 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2011

	Share capital KShs'000	Share premium KShs'000	Statutory credit risk reserve KShs'000	Translation reserve KShs'000	Available-for sale reserve KShs'000	Proposed dividend KShs'000	Retained earnings KShs'000	Total KShs'000
At 1 January 2010	2,217,778	7,297,986	104,670	(119,897)	347,908	2,217,778	10,503,989	22,570,212
Profit for the year	-	-	-	-	-	-	7,177,973	7,177,973
Other comprehensive income	-	-	-	(278,084)	(122,552)	-	-	(400,636)
Transfer to statutory credit risk reserve	-	-	40,959	-	-	-	(40,959)	-
	2,217,778	7,297,986	145,629	(397,981)	225,356	2,217,778	17,641,003	29,347,549
Transactions with owners								
recorded directly in equity								
Dividend paid - 2009	-	-	-	-	-	(2,217,778)	-	(2,217,778)
Proposed dividend - 2010	-	-	-	-	-	3,687,825	(3,687,825)	-
Rights issued, net of issue costs	732,482	11,267,518	-	-	-	-	-	12,000,000
	732,482	11,267,518	-	-	-	1,470,047	(3,687,825)	9,782,222
	2,950,260	18,565,504	145,629	(397,981)	225,356	3,687,825	13,953,178	39,129,771
At 1 January 2011	2,950,260	18,565,504	145,629	(397,981)	225,356	3,687,825	13,953,178	39,129,771
Profit for the year	-	-	-	-	-	-	10,981,046	10,981,046
Other comprehensive income	-	-	-	(193,666)	(2,208,502)	-	-	(2,402,168)
Transfer to statutory credit risk reserve	-	-	1,720,464	-	-	-	(1,720,464)	-
	2,950,260	18,565,504	1,866,093	(591,647)	(1,983,146)	3,687,825	23,213,760	47,708,649
Transactions with owners								
recorded directly in equity								
Dividend paid - 2010	-	-	-	-	-	(3,687,825)	-	(3,687,825)
Proposed dividend - 2011	-	-	-	-	-	5,492,180	(5,492,180)	-
Employee shares option exercised	18,486	325,717	-	-	-	-	-	344,203
	18,486	325,717	-	-	-	1,804,355	(5,492,180)	(3,343,622)
	2,968,746	18,891,221	1,866,093	(591,647)	(1,983,146)	5,492,180	17,721,580	44,365,027

The notes set out on pages 73 to 121 form an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY OF THE BANK

FOR THE YEAR ENDED 31 DECEMBER 2011

	Share capital KShs'000	Share premium KShs'000	Statutory credit risk reserve KShs'000	Available-for sale reserve KShs'000	Proposed dividend KShs'000	Retained earnings KShs'000	Total KShs'000
At 1 January 2010	2,217,778	7,297,986	86,215	347,908	2,217,778	10,230,250	22,397,915
Profit for the year	-	-	-	-	-	8,818,860	8,818,860
Other comprehensive income	-	-	-	(122,552)	-	-	(122,552)
Transfer to statutory credit risk reserve	-	-	(26,787)	-	-	26,787	-
	2,217,778	7,297,986	59,428	225,356	2,217,778	19,075,897	31,094,223
Transactions with owners recorded directly in equity							
Rights issue, net of issue costs	732,482	11,267,518	-	-	-	-	12,000,000
Dividend paid - 2009	-	-	-	-	(2,217,778)	-	(2,217,778)
Proposed dividend - 2010	-	-	-	-	3,687,825	(3,687,825)	-
	732,482	11,267,518	-	-	1,470,047	(3,687,825)	9,782,222
At 31 December 2010	2,950,260	18,565,504	59,428	225,356	3,687,825	15,388,072	40,876,445
At 1 January 2011	2,950,260	18,565,504	59,428	225,356	3,687,825	15,388,072	40,876,445
Profit for the year	-	-	-	-	-	9,838,337	9,838,337
Other comprehensive income	-	-	-	(2,208,502)	-	-	(2,208,502)
Transfer to statutory credit risk reserve	-	-	1,457,708	-	-	(1,457,708)	-
	2,950,260	18,565,504	1,517,136	(1,983,146)	3,687,825	23,768,701	48,506,280
Transactions with owners recorded, directly in equity							
Employee shares option exercised	18,486	325,717	-	-	-	-	344,203
Dividend paid - 2010	-	-	-	-	(3,687,825)	-	(3,687,825)
Proposed dividend - 2011	-	-	-	-	5,492,180	(5,492,180)	-
	18,486	325,717	-	-	1,804,355	(5,492,180)	(3,343,622)
At 31 December 2011	2,968,746	18,891,221	1,517,136	(1,983,146)	5,492,180	18,276,521	45,162,658

The notes set out on pages 73 to 121 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	2011 KShs'000	2010 KShs'000
Net cash flows from/(used in) operating activities	36(a)	19,447,305	(2,067,962)
Tax paid	14(b)	(5,793,529)	(1,425,520)
Investing activities			
Proceeds from disposal of property and equipment		359,151	20,128
Purchase of intangible assets	25	(581,782)	(389,156)
Purchase of operating lease rentals	27	(2,769)	-
Purchase of property and equipment	26(a)	(1,732,186)	(1,903,559)
Net cash flows used in investing activities		(1,957,586)	(2,272,587)
Financing activities			
Net proceeds from additional shares floated		344,203	12,000,000
Borrowing	33	8,525,000	-
Dividends paid	16	(3,687,825)	(2,217,778)
Net cash flows from financing activities		5,181,378	9,782,222
Increase in cash and cash equivalents		16,877,568	4,016,153
Effects of exchange rate changes on translation of foreign operation		(76,894)	(278,084)
Cash and cash equivalents at the beginning of the year		25,130,742	21,392,673
Cash and cash equivalents at the end of the year	36(b)	41,931,416	25,130,742

The notes set out on pages 73 to 121 form an integral part of these financial statements.

STATEMENT OF CASH FLOWS OF THE BANK

FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	2011 KShs'000	2010 KShs'000
Net cash flows from/(used in) operating activities	36(a)	12,082,725	(12,812,076)
Tax paid	14(b)	(5,754,505)	(1,315,529)
Investing activities			
Proceeds from disposal of property and equipment		343,790	8,130
Purchase of intangible assets	25	(581,123)	(336,108)
Purchase of property and equipment	26(b)	(1,075,049)	(1,089,930)
Investment in subsidiaries	28	(1,854,906)	(1,580,773)
Net cash flows used in investing activities		(3,167,288)	(2,998,681)
Financing activities			
Net proceeds from additional shares floated		344,203	12,000,000
Borrowing	33	8,525,000	-
Dividends paid	16	(3,687,825)	(2,217,778)
Net cash flows from financing activities		5,181,378	9,782,222
Increase/(decrease) in cash and cash equivalents		8,342,310	(7,344,064)
Cash and cash equivalents at the beginning of the year		6,754,730	14,098,794
Cash and cash equivalents at the end of the year	36(b)	15,097,040	6,754,730

The notes set out on pages 73 to 121 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2011

1. REPORTING ENTITY

Kenya Commercial Bank Limited, a financial institution licensed under the Kenyan Banking Act (Chapter 488), provides corporate and retail banking services in various parts of the country.

The Bank is incorporated in Kenya under the Kenyan Companies Act and has subsidiaries in Kenya, Southern Sudan, Tanzania, Uganda and Rwanda. The consolidated financial statements of the Bank as at and for the year ended 31 December 2011 comprise the Bank and its subsidiaries (together referred to as the "Group" and individually referred to as the "Bank") and the Group interest in associates. The address of its registered office is as follows:

Kencom House

Moi Avenue
PO Box 48400 - 00100
Nairobi, Kenya

The Bank has a 100% ownership in Kenya Commercial Finance Company Ltd, Savings & Loan Kenya Ltd, Kenya Commercial Bank Nominees Ltd, Kencom House Ltd, KCB (Tanzania) Ltd, KCB Sudan Ltd, KCB Rwanda SA, KCB Bank Uganda Ltd and a 45% ownership in United Finance Ltd.

The shares of the Bank are listed on the Nairobi Securities Exchange, Uganda Securities Exchange, Dar-es-Salaam Stock Exchange, and Rwanda Stock Exchange.

2. BASIS OF PREPARATION

(a) Statement of compliance

The consolidated financial statements of the Bank and its subsidiaries as well as the separate financial statements of the Bank, together referred to as "the financial statements", have been prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB) and the Kenyan Companies Act.

The financial statements for the year ended 31 December 2011 were authorized for issue by the directors on 1st March 2012.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following:

- Financial instruments are measured at fair value through profit or loss;

- Available-for-sale financial assets are measured at fair value;
- Liabilities for cash-settled share-based payment arrangements are measured at fair value;
- Recognized financial assets and financial liabilities designated as hedged items in qualifying fair value hedge relationships are adjusted for changes in fair value attributable to the risk being hedged; and
- The liability for defined benefit obligations is recognized as the present value of the defined benefit obligation less the net total of the plan assets, plus unrecognized actuarial gains less unrecognized past service cost and unrecognized actuarial losses.

(c) Functional and presentation currency

The financial statements are presented in Kenya Shillings (KShs), which is the Bank's functional currency. Except as otherwise indicated, financial information presentation in Kenya shillings has been rounded to the nearest thousand (KShs'000).

(d) Going concern

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

(e) Use of estimates and judgments

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

2. BASIS OF PREPARATION (Continued)

(e) Use of estimates and judgments (Continued)

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

In particular, information about significant areas of estimation and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are described in note 5.

3. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements have been applied consistently across the Group entities and to all periods presented in these financial statements.

(a) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and its subsidiaries and associates for the year ended 31 December 2011. The subsidiaries and associates are shown in note 28.

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The financial statements have been prepared using uniform accounting policies for like transactions and other events in similar circumstances.

(ii) Associates

Associates are entities in which the Group has significant influence, but not control over the financial and operational policies.

Significant influence is presumed to exist when the Group holds between 20 and 50 per cent of the voting power of another entity. The Group's investment in its associate is accounted for using the equity method and is recognized initially at cost. The cost of the investment includes transaction costs.

The consolidated financial statements include the Group's share of profit or loss and other comprehensive income of the equity accounted investee, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases.

When the Group's share of losses exceeds its interest in an equity accounted investee, the carrying amount of the investment including any long-term interests that form part thereof, is reduced to zero, and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the investee.

(iii) Transactions eliminated on consolidation

Intra-group balances and income and expenses (except for foreign currency transaction gains or losses) arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

(b) Foreign currencies

The financial statements are presented in Kenya Shillings, which is the Bank's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Transactions in foreign currencies during the year are converted into the respective functional currencies at rates prevailing at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the exchange rates ruling at the reporting date. The resulting differences from conversion are recognised in the profit and loss account in the year in which they arise.



NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Foreign currencies (Continued)

Non-monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate ruling at the transaction date.

As at the reporting date, the assets and liabilities of foreign subsidiaries are translated into Kenya Shillings at the rate of exchange ruling at the reporting date, and their income statements are translated at the weighted average exchange rates for the period. Exchange differences arising on translation are recognized in other comprehensive income and accumulated in equity in the translation reserve. On disposal of a foreign entity, the deferred cumulative amount recognized in equity relating to that particular foreign operation is reclassified from equity to profit or loss when the gain or loss on disposal is recognized.

(c) Recognition of income and expense

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific criteria must be met before revenue is recognized:

(i) Interest income and expense

For all financial instruments measured at amortized cost and interest bearing financial instruments classified as available-for-sale financial instruments, interest income or expense is recognized at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recognized as interest income or expense.

(ii) Dividend income

Dividend income is recognized when the Group's right to receive payment is established, which in the case of quoted securities is the ex-dividend date.

(iii) Fees and commission income

Fees and commissions are generally recognized on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognized as an adjustment to the effective interest rate on the loan. Commission and fees arising from negotiating, or participating in the negotiation of a transaction for a third party is recognized on completion of the underlying transaction.

Other fees and commission income including account servicing fees, investment management fees, sales commission, placement fees and syndication fees, are recognized as the related services are performed. Other fees and commission expense relate mainly to transaction and services fee, which are expensed as the services are received.

(iv) Rental income

Rental income in respect of operating leases is accounted for on a straight-line basis over the lease terms on ongoing leases.

(v) Foreign exchange income

Foreign exchange income comprises gains less losses related to trading assets and liabilities and includes all realized and unrealized fair value changes, interest and foreign exchange differences.

(d) Income tax expense

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized directly in equity or other comprehensive income, in which case it is recognized in equity or in other comprehensive income.

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

Deferred tax is recognized on all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes,

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(d) Income tax expense (Continued)

except differences relating to the initial recognition of assets or liabilities in a transaction that is not a business combination and which affects neither accounting nor taxable profit.

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 by the reporting date. A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized.

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 realized.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax 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 assets and liabilities on a net basis or their tax assets and liabilities will be realized simultaneously.

(e) Financial instruments

(i) Recognition

The Group initially recognises cash, amounts due from/to due to group companies, loans and advances, deposits, debt securities and subordinated liabilities on the date they are originated. All other financial assets and liabilities (including assets and liabilities designated at fair value through profit or loss) are initially recognised on the trade date at which the group becomes a party to the contractual provisions of the instrument. A financial asset or financial liability is initially measured at fair value plus (for an item not subsequently measured at fair value through profit or loss) transaction costs that are directly attributable to its acquisition or issue.

(ii) Derecognising

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expires, or it transfers

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

The Group enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the statement of financial position. Transfers of assets with retention of all or substantially all risks and rewards include, for example, securities lending and repurchase transactions. If, as a result of a transfer, a financial asset is derecognised in its entirety but the transfer results in the Group obtaining a new financial asset or assuming a new financial liability, the Group recognises the new financial asset or financial liability at fair value.

Where a financial asset is derecognised in its entirety, the difference between the carrying amount and the sum of the consideration received together with any gain or loss previously recognised in other comprehensive income, are recognised in profit or loss. The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

(iii) Offsetting of financial assets and liabilities

Financial assets and liabilities are offset and the net amount reported on the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted under IFRSs, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Financial instruments (Continued)

(iv) Fair value of financial instruments

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

The determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations for financial instruments traded in active markets. For all other financial instruments fair value is determined by using valuation techniques. Valuation techniques include net present value techniques, the discounted cash flow method, comparison to similar instruments for which market observable prices exist, and valuation models. The Group uses widely recognised valuation models for determining the fair value of common and simpler financial instruments like options, interest rate and currency swaps. For these financial instruments, inputs into models are market observable.

For more complex instruments, the Group uses proprietary models, which are usually developed from recognised valuation models. Some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions.

When entering into a transaction, the financial instrument is recognised initially at the transaction price, which is the best indicator of fair value, although the value obtained from the valuation model may differ from the transaction price.

This initial difference, usually an increase, in fair value indicated by valuation techniques is recognised in profit or loss depending on the individual facts and circumstances of each transaction and not later than when the market data becomes observable.

The value produced by a model or other valuation techniques is adjusted to allow for a number of factors as appropriate, because valuation techniques cannot appropriately

reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments carried at fair value on the statement of financial position.

(v) Amortised cost measurement

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

(vi) Identification and measurement of impairment of financial assets

At each reporting date the Group assesses whether there is objective evidence that financial assets carried at amortised cost are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the Group.

The Group considers evidence of impairment for loans and advances and investment securities measured at amortised costs at both a specific asset and collective level.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Financial instruments (Continued)

(vi) Identification and measurement of impairment of financial assets (Continued)

All individually significant loans and advances and investment securities measured at amortised cost are assessed for specific impairment. All individually significant loans and advances and investment securities measured at amortised cost found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified.

Loans and advances and investment securities measured at amortised cost that are not individually significant are collectively assessed for impairment by grouping together loans and advances and investment securities measured at amortised cost with similar risk characteristics.

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

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

The Group writes off loans and advances and investment securities when they are determined to be uncollectible.

(vii) Investments held for trading

Investments held for trading are those which were either acquired for generating a profit from short-term fluctuations in price or dealer's margin, or are securities included in a portfolio in which a pattern of short-term profit-taking exists. Investments held for trading are subsequently re-measured at fair value based on quoted bid prices or dealer price quotations, without any deduction for transaction costs. All related realized and unrealized gains and losses are included in profit or loss. Interest earned whilst holding held for trading investments is reported as interest income.

(viii) Cash and cash equivalents

Cash and cash equivalents comprise balances with less than three months maturity from the date of acquisition, including: notes and coins on hand, unrestricted balances deposited with the Central Bank of Kenya and highly liquid assets, subject to insignificant risk of changes in their fair value. Cash and cash equivalents are carried at amortized cost in the statement of financial position.

(ix) Foreign exchange forward and spot contracts

Foreign exchange forward and spot contracts are classified as held for trading. They are marked to market and are carried at their fair value. Fair values are obtained from discounted cash flow models which are used in the determination of the foreign exchange forward and spot contract rates. Gains and losses on foreign exchange forward and spot contracts are included in foreign exchange income as they arise.

(f) Property and equipment

(i) Recognition and measurement

Items of property and equipment are measured at cost, less accumulated depreciation and accumulated impairment losses. Costs include expenditure that is directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(f) Property and equipment (Continued)

(i) Recognition and measurement (Continued)

Property and equipment is de-recognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Gains and losses arising on disposal of an item of property and equipment are determined by comparing the net proceeds from disposal with the carrying amount of the item and are recognized net within 'other operating income' in profit or loss.

(ii) Depreciation

Depreciation is recognized in profit or loss on a straight line basis over the estimated useful lives of each part of property and equipment. The annual depreciation rates in use are:

Freehold land	Nil
Leasehold improvements	Rates based on the shorter of the lease term or estimated useful lives
Motor vehicles	25%
Furniture and fittings	10%
Office equipment	20%
Computers	20%

The assets residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each reporting date. Changes in the expected useful life are accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates.

(iii) Subsequent costs

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

(g) Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditure is recognized in profit or loss in the year in which the expenditure is incurred. Intangible assets with finite lives are amortized on a straight-line basis in profit or loss over their estimated useful economic lives, from the date that they are available for use.

The amortization method, useful life and the residual value are reviewed at each financial year-end and adjusted if appropriate. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in profit or loss in the expense category consistent with the function of the intangible asset.

The useful lives of intangible assets are assessed to be either finite or indefinite. Costs associated with maintaining computer software programmes are recognised as an expense as incurred. However, expenditure that enhances or extends the benefits of computer software programmes beyond their original specifications and lives is recognized as a capital improvement and added to the original cost of the software. Computer software development costs recognized as assets are amortised using the straight-line method over a period of five years. There are no intangible assets with indefinite useful lives.

(h) Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(h) Leases (Continued)

Leases, where a significant portion of the risks and rewards of ownership are retained by the lessor, are classified as operating leases. Payments made under operating leases are charged to the profit and loss account on a straight-line basis over the period of the lease. Leases where substantially all the risks and rewards of ownership of an asset are transferred to the Lessee are classified as finance leases. Upon recognition the leased asset is measured at an amount equal to or lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset as follows:

(i) Operating lease

The total payments made under operating leases are charged to profit or loss on a straight-line basis over the period of the lease. 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.

(ii) Finance lease

When assets are held subject to a finance lease, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

(i) Impairment of non-financial assets

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

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell.

In assessing value in use, the estimated future cash

flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the profit or loss account. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro-rata basis.

(j) Investment in subsidiaries

Investments in subsidiary companies are carried at cost which is the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the acquirer, in exchange for control of the acquiree. The carrying amount is reduced to recognise any impairment in the value of individual investments. The impairment loss is taken to profit or loss.

(k) Investment in associates

The consolidated financial statements include the Group's share of the income and expenses and equity movements of equity accounted investees, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the investee. Consolidation adjustments are also made to ensure consistency with the Group's accounting policies. Associates are accounted for using the equity method and are initially recognised at cost.

(l) Provisions

A provision is recognised when the Group has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(l) Provisions (Continued)

Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to that liability.

(m) Employee benefit cost

The Group operates both a defined contribution plan and defined benefit plan.

(i) Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an employee benefit expense in profit or loss in the periods during which services are rendered by employees. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available. Contributions to a defined contribution plan that are due more than 12 months after the end of the reporting period in which the employees rendered the service are discounted to their present value at the reporting date.

(ii) Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. Any unrecognised past service costs and the fair value of any plan assets are deducted. The discount rate is the yield at the reporting date on AA credit-rated bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

To determine the net amount in the statement of financial position, any actuarial gains and losses that have not been recognised because of application of the 'corridor' approach described below are added or deducted as appropriate and unrecognised past service costs are deducted.

The Group recognises a portion of actuarial gains and losses that arise in calculating the Group's obligation in respect of a plan in profit or loss over the expected average remaining working lives of the employees participating in the plan. The portion is determined as the extent to which any cumulative unrecognised actuarial gain or loss at the end of the previous reporting period exceeds 10 per cent of the greater of the present value of the defined benefit obligation and the fair value of plan assets (the corridor). Otherwise, the actuarial gains and losses are not recognised.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised in profit or loss on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in profit or loss.

When the calculations above result in a benefit to the Group, the recognised asset is limited to the net total of any cumulative unrecognised actuarial losses and past service costs and the present value of any economic benefits available in the form of any refunds from the plan or reductions in future contributions to the plan. In order to calculate the present value of economic benefits, consideration is given to any minimum funding requirements that apply to any plan in the Group. An economic benefit is available to the Group if it is realisable during the life of the plan or on settlement of the plan liabilities.

(iii) Short-term benefits

Short-term benefits consist of salaries, bonuses and any non-monetary benefits such as medical aid contributions and free services. They exclude equity based benefits and termination benefits.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(iii) *Short-term benefits (Continued)*

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

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

(iv) *Termination benefits*

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

(v) *Share-based payment transactions*

The grant date fair value of equity-settled share-based payment awards (i.e. stock options) granted to employees is recognized as an employee expense, with a corresponding increase in equity, over the period in which the employees unconditionally become entitled to the awards. The amount recognized as an expense is adjusted to reflect the number of share awards that do meet the related service and non-market performance conditions at the vesting date.

The fair value of the amount payable to employees in respect of share appreciation rights that are settled in cash is recognized as an expense with a corresponding increase in liabilities over the period in which the employees unconditionally become entitled to payment.

The liability is remeasured at each reporting date and at settlement date. Any changes in the fair value of the liability are recognized as personnel expense in profit or loss.

(n) **Fiduciary assets**

When the Group acts in a fiduciary capacity such as a nominee or agent, assets and income arising thereon with related undertakings to return such assets to customers are excluded from these financial statements.

(o) **Contingent liabilities**

Letters of credit, acceptances, guarantees and performance bonds are disclosed as contingent liabilities. Estimates of the outcome and the financial effect of contingent liabilities is made by management based on the information available up to the date that the financial statements are approved for issue by the directors.

(p) **Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the respective assets. All other borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Borrowing costs are recognised as an expense when incurred.

(q) **Earnings per share**

Basic and diluted earnings per share (EPS) data for ordinary shares are presented in the financial statements. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, if any.



NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(r) Dividends

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

(s) Sale and repurchase agreements

Securities sold under sale and repurchase agreements (Repos) are retained in the financial statements with the counterparty liability included in amounts due to banking institutions.

Securities purchased from the Central Bank of Kenya under agreement to resell (reverse Repos), are disclosed as treasury bills as they are held to maturity after which they are repurchased and are not negotiable or discounted during the tenure. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

(t) Related parties

In the normal course of business, the Bank has entered into transactions with related parties. The related party transactions are at arm's length.

(u) Operating segments

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, whose operating results are reviewed regularly by the Group's Management Executive Committee (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

(v) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2011, and have not been applied in preparing these consolidated financial statements. These are summarised below and are not expected to have a significant impact on the consolidated financial statements of the Group:

- *IFRS 9 Financial Instruments. IFRS 9 will become mandatory for the Group's 2015 consolidated financial statements.*
- *IFRS 10 Consolidated Financial Statements (effective for annual periods beginning on or after 1 January 2013).*
- *IFRS 11 Joint Arrangements (effective for annual periods beginning on or after 1 January 2013).*
- *IFRS 12 Disclosure of Interests in Other Entities (effective for annual periods beginning on or after 1 January 2013).*
- *IFRS 13 Fair Value Measurement (effective for annual periods beginning on or after 1 January 2013).*
- *IAS 19 Employee Benefits (Amended) (effective for annual periods beginning on or after 1 January 2013).*
- *IAS 27 (2011) Separate Financial Statements. (Effective 1 January 2013)*
- *IAS 28 (2011) Investments in Associates and Joint Ventures. (Effective 1 January 2013)*
- *Amendments to IAS 1 presentation of items of other comprehensive income (effective 1 January 2012)*
- *Amendments to IAS 12 Deferred tax: Recovery of underlying assets statements (effective 1 January 2012)*
- *Amendments to IFRS 7 Disclosures: - Transfer of financial assets (effective for annual period beginning 1 July 2011).*

4. FINANCIAL RISK MANAGEMENT

The Group's activities expose it to a variety of financial risks, including credit risk, liquidity risk, market risks, operational risks and interest rates risks. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board of Directors of the Group has established the Credit, Audit and Compliance, Risk Management, New Markets, Human Resources and Procurement Committees, which are responsible for developing and monitoring the Group risk management policies in their specified areas.

4. FINANCIAL RISK MANAGEMENT (Continued)

All Board committees have both executive and non-executive members and report regularly to the Board of Directors on their activities. The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls and to monitor risks and adherence to limits.

Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Risk Committee is responsible for monitoring compliance with the Group's risk management policies and procedures and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Group. The Committee is assisted in these functions by a Risk and Compliance department which undertake reviews of risk management controls and procedures, the results of which are reported to the Risk Committee.

(a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's loans and advances to customers, placement and balances with other counterparties and investment securities. It arises from lending and other activities undertaken by the Group. For risk management reporting purposes, the Group considers and consolidates all elements of credit risk exposure.

(i) Management of credit risk

The Board of Directors has delegated responsibility for the management of credit risk to its Credit Committee. A separate credit department, reporting to the Credit Committee, is responsible for oversight of the Group's credit risk, including:

- Formulating credit policies in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements;
- Establishing the authorisation structure

for the approval and renewal of credit facilities. Authorisation limits are allocated to business unit credit managers. Larger facilities require approval by the Board of Directors;

- Reviewing and assessing credit risk. The credit department assesses all credit exposures in excess of designated limits, prior to facilities being committed to customers by the business unit concerned. Renewals and reviews of facilities are subject to the same review process;
- Limiting concentrations of exposure to counterparties, geographies and industries (for loans and advances), and by issuer, credit rating band, market liquidity and country (for investment securities);
- Developing and maintaining the Group's risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management attention on the risks. The risk grading system is used in determining where impairment provisions may be required against specific credit exposures. The current risk grading framework consists of five grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation;
- Reviewing compliance of business units with agreed exposure limits, including those for selected industries and product types. Regular reports are provided to the Credit Committee on the credit quality of local portfolios and appropriate corrective action is taken;
- Providing advice, guidance and specialist skills to business units to promote best practice throughout the Group in the management of credit risk;
- Each business unit is required to implement the Group's credit policies and procedures. Each business unit has a credit manager who reports on all credit related matters to local management and the Credit Committee. Each business unit is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios, including those subject to central approval; and

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (Continued)

(i) Management of credit risk (Continued)

- Regular audits of business units and the Group's credit processes are undertaken by Internal Audit Department.

(ii) Credit risk measurement

The Group assesses the probability of default of customer or counterparty using internal rating scale tailored to the various categories of counterparty. The rating scale has been developed internally and combines data analysis with credit officer judgment and is validated, where appropriate, by comparison with externally available information. Customers of the Group are segmented into five rating classes. The Group's rating scale, which is shown below, reflects the range of default probabilities defined for each rating class. This means that, in principle, exposures migrate between classes as the assessment of their probability of default changes.

The Group regularly validates the performance of the rating and their predictive power with regard to default events.

The Group's internal ratings scale is as follows:

Grade 1 - Normal risk

Grade 2 - Watch risk

Grade 3 - Sub standard risk

Grade 4 - Doubtful risk

Grade 5 - Loss

(iii) Impairment and provisioning policies

The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in its loans and advances portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures. The second component is in respect of losses that have been incurred but have not been identified in relation to the loans and advances portfolio that is not specifically impaired.

The impairment provision recognised in the statement of financial position at year-end is derived from each of the five internal rating grades.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (Continued)

The Group exposure to credit risk is analysed as follows:

	GROUP		BANK	
	2011 KShs '000	2010 KShs '000	2011 KShs '000	2010 KShs '000
Individually impaired				
Grade 3	2,897,970	3,101,867	2,442,667	2,226,705
Grade 4	5,057,418	6,311,868	4,453,564	5,994,003
Grade 5	4,272,876	5,169,647	3,518,717	4,833,019
Gross amount	12,228,264	14,583,382	10,414,948	13,053,727
Allowance for impairment	(6,466,159)	(8,587,097)	(5,724,058)	(8,178,514)
Carrying amount	5,762,105	5,996,285	4,690,890	4,875,213
Collectively impaired				
Grade 1	181,797,780	132,804,585	165,376,432	124,423,554
Grade 2	12,690,583	11,377,323	11,042,282	9,949,137
Gross amount	194,488,363	144,181,908	176,418,714	134,372,691
Allowance for impairment	(1,525,549)	(2,064,829)	(1,265,617)	(1,903,336)
	192,962,814	142,117,079	175,153,097	132,469,355
Total Carrying amount	198,724,919	148,113,364	179,843,987	137,344,568

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (Continued)

(iii) Impairment and provisioning policies (Continued)

Loans and advances graded 3, 4 and 5 in the Group's internal credit risk grading system include items that are individually impaired. These are advances for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan agreements.

Loans and advances graded 1 and 2 are not individually impaired. Allowances for impairment losses for these loans and advances are assessed collectively.

The Group also complies with Central Banks' prudential guidelines on general and specific provisioning. Additional provisions for loan losses required to comply with the requirements of Central Banks' prudential guidelines are transferred to statutory credit risk reserve.

The internal rating scale assists management to determine whether objective evidence of impairment exists, based on the following criteria set out by the Group:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral.

The Group's policy requires the review of individual financial assets regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the impairment at reporting date on a case-by-case basis, and are applied to all individually significant accounts.

The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

(iv) Credit - related commitment risk

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

(v) Write-off policy

The Group writes off a loan balance as and when the Credit Committee determines that the loans are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower's financial position such that the borrower can no longer pay the obligation or that proceeds from collateral will not be sufficient to pay back the entire exposure.

(vi) Collateral on loans and advances

The Group holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing and generally are not updated except when a loan is individually assessed as impaired.

(vii) Concentration of credit risk

The Group's financial instruments do not represent a concentration of credit risk because the Group deals with a variety of customers and its loans and advances are structured and spread among a number of customers. The Group monitors concentrations of credit risk by sector.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(a) Credit risk (Continued)

(vii) Concentration of credit risk (Continued)

An analysis of concentrations of credit risk at the reporting date is shown below:

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Construction	33,722,489	22,655,575	31,618,634	21,800,273
Micro credit	60,271,341	45,092,890	55,327,106	45,065,735
Agriculture	10,677,484	9,174,953	9,584,416	8,590,672
Small and medium enterprises	22,505,749	19,969,822	21,361,975	16,232,352
Corporate	79,539,564	61,872,050	68,941,531	55,737,386
	206,716,627	158,765,290	186,833,662	147,426,418

(viii) Fair value of collateral held

The Group holds collateral against loans and advances to customers in the form of cash, residential, commercial and industrial property. The Group also enters into collateralised reverse purchase agreements. Risk mitigation policies control the approval of collateral types. Collateral is valued in accordance with the Group's risk mitigation policy, which prescribes the frequency of valuation for different collateral types. The valuation frequency is driven by the level of price volatility of each type of collateral.

Collateral held against impaired loans is maintained at fair value. The valuation of collateral is monitored regularly and is back tested at least annually.

Collateral generally is not held over loans and advances to banks, except when securities are held as part of reverse purchase and securities borrowing activity. Collateral usually is not held against investment securities, and no such collateral was held as at 31 December 2011 and 2010.

An estimate of fair values of collaterals held against loans and advances to customers at the end of the year was as follows:

	GROUP		BANK	
	2011 KShs '000	2010 KShs '000	2011 KShs '000	2010 KShs '000
Impaired loans	5,762,000	5,996,000	4,691,000	4,875,000
Performing loans	152,000,000	101,000,000	135,000,000	94,000,000
	157,762,000	106,996,000	139,691,000	98,875,000



NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(b) Liquidity risk

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

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

The Group's treasury maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Group as a whole. The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions.

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to deposits from customers.

Details of the reported Group's ratio of net liquid assets to deposits from customers at the reporting date and during the reporting year were as follows:

	2011	2010
At close of the year	31.3%	30.74%
Average for the year	28.2%	35.49%
Maximum for the year	35.0%	39.32%
Minimum for the year	20.7%	30.20%

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(b) Liquidity risk (Continued)

The table below summarizes the Group's liquidity risk as at 31 December 2011 and 31 December 2010:

As at 31 December 2011	Up to 1 month KShs'000	1-3 months KShs'000	3-12 months KShs'000	1-5 years KShs'000	Over 5 years KShs'000	Total KShs'000
Cash and balances with Central Banks	39,073,197	1,680,362	1,580,849	373,608	-	42,708,016
Due from banks	25,812,084	-	-	-	-	25,812,084
Held for trading investments	367,938	-	-	-	-	367,938
Available for sale investments	-	-	-	8,529,031	675,470	9,204,501
Held to maturity investments	60,038	323,328	4,170,474	15,460,537	16,417,820	36,432,197
Loans and advances to customers	20,859,253	10,149,645	16,513,547	70,841,071	80,361,403	198,724,919
Other assets-Uncleared effect	-	-	866,225	-	-	866,225
Total financial assets	86,172,510	12,153,335	23,131,095	95,204,247	97,454,693	314,115,880
Due to banks	14,105,149	-	-	-	-	14,105,149
Other customer deposits	188,092,210	32,923,178	30,973,414	7,320,047	-	259,308,849
Other liabilities-Bills payable	-	-	731,796	-	-	731,796
Long term debt	-	-	-	6,200,000	2,325,000	8,525,000
Total financial liabilities	202,197,359	32,923,178	31,705,210	13,520,047	2,325,000	282,670,794
Net liquidity gap	(116,024,849)	(20,769,843)	(8,574,115)	81,684,200	95,129,693	31,445,086

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(b) Liquidity risk (Continued)

As at 31 December 2010	Up to 1 month KShs'000	1-3 months KShs'000	3-12 months KShs'000	1-5 years KShs'000	Over 5 years KShs'000	Total KShs'000
Cash and balances with Central Banks	14,437,833	2,752,068	9,208,199	599,723	-	26,997,823
Due from banks	3,959,957	6,251,051	-	-	-	10,211,008
Held for trading investments	847,876	-	-	-	-	847,876
Available for sale investments	-	-	-	4,903,188	959,300	5,862,488
Held to maturity investments	2,138,342	4,589,408	5,631,555	12,078,802	18,960,027	43,398,134
Loans and advances to customers	12,582,423	5,979,303	12,567,391	65,441,213	51,543,034	148,113,364
Other assets-Uncleared effects	-	-	1,273,624	-	-	1,273,624
Total financial assets	33,966,431	19,571,830	28,680,769	83,022,926	71,462,361	236,704,317
Due to banks	11,056,967	-	-	-	-	11,056,967
Other customer deposits	165,664,847	5,790,903	19,560,235	5,958,666	-	196,974,651
Other liabilities-Bills payable	-	-	706,405	-	-	706,405
Total liabilities and shareholders' funds	176,721,814	5,790,903	20,266,640	5,958,666	-	208,738,023
Net liquidity gap	(142,755,383)	13,780,927	8,414,129	77,064,260	71,462,361	27,966,294

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(c) Currency risk

The Group takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure by currency and in total for both overnight and intra-day positions which are monitored daily and hedging strategies used to ensure that positions are maintained within the established limits.

Transactions in foreign currency are recorded at the rate in effect at the date of the transaction. The Group translates monetary assets and liabilities denominated in foreign currencies at the rate of exchange in effect at the reporting date. The Group records all gains or losses on changes in currency exchange rates in profit or loss.

The table below summarizes the foreign currency exposure as at 31 December 2011 and 31 December 2010:

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Assets in foreign currencies	160,310,219	99,366,461	138,975,983	91,848,193
Liabilities in foreign currencies	(160,243,499)	(99,411,684)	(140,111,426)	(92,095,348)
Net foreign currency exposure at the end of the year	66,720	(45,223)	(1,135,443)	(247,155)

The following table demonstrates the sensitivity to a reasonably possible change in the below mentioned exchange rates, with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities).

Increase/decrease in exchange rate		Effect on profit before tax	
		2011 KShs' 000	2010 KShs' 000
USD	10%	78,624	13,002
GBP	10%	11,634	7,011
EUR	10%	6,378	3,170

(d) Interest rate risk

Interest rate risk is the risk that the future cash flows of financial instruments will fluctuate because of changes in the market interest rates. Interest margin may increase as a result of such changes but may reduce losses in the event that unexpected movement arises. The Group closely monitors interest rate movements and seeks to limit its exposure by managing the interest rate and maturity structure of assets and liabilities carried on the statement of financial position.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011 (Continued)

4. FINANCIAL RISK MANAGEMENT (Continued)

(d) Interest rate risk (Continued)

The table below shows interest rate sensitivity position of the Group at 31 December based on the earlier of maturity or re-pricing dates. Items not recognized on the statement of financial position do not pose any significant interest rate risk to the Group.

As at 31 December 2011	Weighted interest rates	Up to 1 month KShs'000	1-3 months KShs'000	3-12 months KShs'000	1-5 years KShs'000	Over 5 years KShs'000	Non-interest bearing KShs'000	Total KShs'000
Cash and balances with Central Banks	-	-	-	-	-	-	42,708,016	42,708,016
Due from banks	27.0%	25,812,084	-	-	-	-	-	25,812,084
Held for trading investments	7.8%	367,938	-	-	-	-	-	367,938
Available for sale investments	8.7%	-	-	-	8,529,031	200,962	474,508	9,204,501
Loans and advances to customers	12.7%	20,859,253	10,149,645	16,513,547	70,841,071	80,361,403	-	198,724,919
Held to maturity investments	7.8%	60,038	323,328	4,170,474	15,460,537	16,417,820	-	36,432,197
Other assets - Uncleared effects	-	-	-	-	-	-	866,225	866,225
Total financial assets		47,099,313	10,472,973	20,684,021	94,830,639	96,980,185	44,048,749	314,115,880
Due to banks	1.0%	14,105,149	-	-	-	-	-	14,105,149
Other customer deposits	1.6%	188,092,210	32,923,178	30,973,414	7,320,047	-	-	259,308,849
Other liabilities - Bills payable	-	-	-	-	-	-	731,796	731,796
Long term debt	2.3%	-	-	-	6,200,000	2,325,000	-	8,525,000
Total financial liabilities		202,197,359	32,923,178	30,973,414	13,520,047	2,325,000	731,796	282,670,794
Interest rate sensitivity gap		(155,098,046)	(22,450,205)	(10,289,393)	81,310,592	94,655,185	43,316,953	31,445,086

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011 (Continued)

4. FINANCIAL RISK MANAGEMENT (Continued)

(d) Interest rate risk (Continued)

As at 31 December 2010	Weighted interest rates	Up to 1 month KShs'000	1-3 months KShs'000	3-12 months KShs'000	1-5 years KShs'000	Over 5 years KShs'000	Non-interest bearing KShs'000	Total KShs'000
Cash and balances with Central Banks	-	-	-	-	-	-	26,997,823	26,997,823
Due from banks	3.0%	3,959,957	6,251,051	-	-	-	-	10,211,008
Held for trading investments	9.6%	847,876	-	-	-	-	-	847,876
Available for sale investments	10.4%	-	-	-	4,903,188	661,835	297,465	5,862,488
Held to maturity investments	8.1%	12,582,423	5,979,303	12,567,391	65,441,213	51,543,034	-	148,113,364
Loans and advances to customers	12.5%	2,138,342	4,589,408	5,631,555	12,078,802	18,960,027	-	43,398,134
Other assets - Uncleared effects	-	-	-	-	-	-	1,273,624	1,273,624
Total financial assets		19,528,598	16,819,762	18,198,946	82,423,203	71,164,896	28,568,912	236,704,317
Due to banks	1.2%	11,056,967	-	-	-	-	-	11,056,967
Other customer deposits	1.1%	165,664,847	5,790,903	19,560,235	5,958,666	-	-	196,974,651
Other liabilities - Bills payable	-	-	-	-	-	-	706,405	706,405
Total financial liabilities		176,721,814	5,790,903	19,560,235	5,958,666	-	706,405	208,738,023
Interest rate sensitivity gap		(157,193,216)	11,028,859	(1,361,289)	76,464,537	71,164,896	27,862,507	27,966,294

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(d) Interest rate risk (Continued)

At 31st December 2011, if there was a 1% interest rate variation, the Group's profit before tax would decrease/increase by KShs. 247.9 million (2010: KShs. 177 million)

(e) Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Group's processes, personnel, technology and infrastructure and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Group's operations and are faced by all business units.

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

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Group standards for the management of operational risk in the following areas:

- Requirements for appropriate segregation of duties, including the independent authorisation of transactions.
- Requirements for the reconciliation and monitoring of transactions.
- Compliance with regulatory and other legal requirements.
- Documentation of controls and procedures.
- Requirements for the yearly assessment of operational risks faced and the adequacy of controls and procedures to address the risks identified.
- Requirements for the reporting of operational losses and proposed remedial action.
- Development of contingency plans.

- Training and professional development.
- Ethical and business standards.
- Risk mitigation, including insurance where this is effective.

Compliance with Group's standards is supported by a programme of regular reviews undertaken by both the Internal Audit and Compliance department. The results of internal audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the Audit Committee and senior management of the Group.

(f) Capital management

The primary objective of the Bank's capital management is to ensure that the Bank complies with capital requirements and maintains healthy capital ratios in order to support its business and to maximise shareholders' value.

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by the Central Bank of Kenya. The Central Bank of Kenya sets and monitors capital requirements for the banking industry as a whole.

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

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

- Core Capital (Tier 1) capital, which includes ordinary share capital, share premium, retained earnings, after deductions for investments in financial institutions, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes; and
- Supplementary Capital (Tier 2) which includes the regulatory reserve.

Various limits are applied to elements of the capital base.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

4. FINANCIAL RISK MANAGEMENT (Continued)

(f) Capital management (Continued)

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

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

	2011 KShs'000	2010 KShs'000
Core Capital (Tier 1):		
Ordinary share capital	2,968,746	2,950,260
Retained earnings	23,768,701	19,075,897
Share premium	18,891,221	18,565,504
Less: Investments in financial institutions	(7,225,759)	(5,370,853)
Total Core Capital	38,402,909	35,220,808
Supplementary Capital (Tier 2):		
Regulatory reserve	1,517,136	59,428
Total regulatory capital	39,920,045	35,280,236
Risk weighted assets	192,939,432	152,310,594

Capital ratios:

Total regulatory capital expressed as a per cent age of total risk-weighted assets	20.7%	23.2%
Core capital expressed as a per cent age of total risk-weighted assets	19.9%	23.1%

The minimum capital ratios, as per the Central Bank of Kenya regulations, are as follows:

Total regulatory capital expressed as a per cent age of total risk-weighted assets	12.0%	12.0%
Core capital expressed as a per cent age of total risk-weighted assets	8.0%	8.0%

As at end of the year, the minimum core capital requirement by Central Bank of Kenya was KShs. 700 million (2010: KShs. 500 million). The Bank was in compliance with all statutory capital requirements as at end of the year.



NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

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5. USE OF ESTIMATES AND JUDGMENTS

In determining the carrying amounts of certain assets and liabilities, the Group makes assumptions of the effects of uncertain future events on those assets and liabilities at the reporting date. The Group's estimates and assumptions are based on historical experience and expectation of future events and are reviewed periodically. This disclosure excludes uncertainty over future events and judgments in respect of measuring financial instruments. Further information about key assumptions concerning the future, and other key sources of estimation uncertainty are set out in the notes.

(a) Impairment losses on loans and advances

The Group loan loss provisions are established to recognize incurred impairment losses either on individual significant loans or within a portfolio of loans and advances.

The Group reviews its loans and advances at each reporting date to assess whether an allowance for impairment should be recognised in profit or loss. In particular, judgment by the directors is required in the estimation of the amount and timing of future cash flows when determining the level of allowance required. Such estimates are based on the assumptions about a number of factors and actual results may differ, resulting in future changes in the allowance.

In addition to specific allowances against individual significant loans and advances, the Group makes a collective impairment allowance against exposures which, although not specifically identified as requiring a specific allowance, have a greater risk of default than when originally granted. This takes into consideration such factors as any deterioration in industry, technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows and past loss experience and defaults based on portfolio trends.

(b) Deferred tax assets

Deferred tax assets are recognized for all unused tax losses to the extent that it is possible that taxable profit will be available against which the losses can be utilized. Significant directors' judgment is required to determine the amount of deferred tax asset that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

(c) Pensions

The cost of the defined benefit pension plan is determined using actuarial valuation. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Due to the long term nature of these plans, such estimates are subject to significant uncertainty.

(d) Property and equipment

Property and equipment is depreciated over its useful life taking into account residual values, where appropriate. The actual lives of the assets and residual values are assessed annually and may vary depending on a number of factors. In reassessing asset lives, factors such as technological innovation, product life cycles and maintenance programmes are taken into account. Residual value assessments consider issues such as future market conditions, the remaining life of the asset and projected disposal values. The rates used are set out on accounting policy 3(f) (ii).

6. FINANCIAL ASSETS AND LIABILITIES

Accounting classification and fair values

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

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

Subsequent to initial recognition, some of the Group's financial instruments are carried at fair value, with changes in fair value either reported within profit or loss or within other comprehensive income until the instrument is sold or becomes impaired.

The fair values of quoted financial instruments in active markets are based on current prices. If the market for a financial instrument is not active including market for unlisted securities, the Group establishes fair value by using valuation techniques.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

6. FINANCIAL ASSETS AND LIABILITIES (Continued)

Accounting classification and fair values (Continued)

These techniques include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Where representative prices are unreliable because of illiquid markets, the determination of fair value may require estimation of certain parameters, which are calibrated against industry standards and observable market data, or the use of valuation models that are based on observable market data. The fair value for the majority of the Group's financial instruments is based on observable market prices or derived from observable market parameters.

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

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have significant effect on the recorded fair value that are not based on observable market data.

The table below shows the classification of financial assets and liabilities at their fair values based on the hierarchy described above.

	Level 1 KShs.000	Level 2 KShs.000	Level 3 KShs.000	Total KShs.000
2011 Group and Bank				
Financial assets:				
Held for trading investments	-	367,938	-	367,938
Available for sale investments	469,743	8,734,758	-	9,204,501
Total financial assets fair valued	469,743	9,102,696	-	9,572,439
2010 Group and Bank				
Financial assets:				
Held for trading investments	-	847,876	-	847,876
Available for sale investments	292,700	5,569,788	-	5,862,488
Total financial assets fair valued	292,700	6,417,664	-	6,710,364

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

6. FINANCIAL ASSETS AND LIABILITIES (Continued)

The table below sets out the carrying amounts of each class of financial assets and liabilities, and their fair values.

	Held for trading KShs. 000	Held to maturity KShs. 000	Loans and receivables KShs. 000	Available for sale KShs. 000	Other amortized cost KShs. 000	Total carrying amount KShs. 000	Fair value KShs. 000
2011-Group							
Assets							
Cash and balances with Central Banks	-	-	42,708,016	-	-	42,708,016	42,708,016
Due from other banks	-	-	25,812,084	-	-	25,812,084	25,812,084
Government and other securities	367,938	36,432,197	-	6,790,693	-	43,590,828	43,590,828
Investment securities	-	-	-	2,413,808	-	2,413,808	2,413,808
Loans and advances to customers	-	-	198,724,919	-	-	198,724,919	198,724,919
Other assets – uncleared effects	-	-	866,225	-	-	866,225	866,225
Total financial assets	367,938	36,432,197	268,111,244	9,204,501	-	314,115,880	314,115,880
Liabilities							
Due to other banks	-	-	-	-	14,105,149	14,105,149	14,105,149
Deposits from customers	-	-	-	-	259,308,849	259,308,849	259,308,849
Other liabilities – bills payable	-	-	-	-	731,796	731,796	731,796
Long term debt	-	-	-	-	8,525,000	8,525,000	8,525,000
Total financial liabilities	-	-	-	-	282,670,794	282,670,794	282,670,794
2010-Group							
Assets							
Cash and balances with Central Banks	-	-	26,997,823	-	-	26,997,823	26,997,823
Due from other banks	-	-	10,211,008	-	-	10,211,008	10,211,008
Government and other securities	847,876	43,398,134	-	3,425,723	-	47,671,733	47,671,733
Investment securities	-	-	-	2,436,765	-	2,436,765	2,436,765
Loans and advances to customers	-	-	148,113,364	-	-	148,113,364	148,113,364
Other assets – uncleared effects	-	-	1,273,624	-	-	1,273,624	1,273,624
Total financial assets	847,876	43,398,134	186,595,819	5,862,488	-	236,704,317	236,704,317
Liabilities							
Due to other banks	-	-	-	-	11,056,967	11,056,967	11,056,967
Deposits from customers	-	-	-	-	196,974,651	196,974,651	196,974,651
Other liabilities – bills payable	-	-	-	-	706,405	706,405	706,405
Total financial liabilities	-	-	-	-	208,738,023	208,738,023	208,738,023

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

7. SEGMENT REPORTING

Reportable segments

The Group's main business comprises of the following reportable segments:

- Retail banking – incorporating banking services such as customer current accounts, savings and fixed deposits to individuals. Retail lending are mainly consumer loans.
- Corporate banking – incorporating banking services such as current accounts, fixed deposits, overdrafts, loans and other credit facilities both in local and foreign currencies.
- Mortgages – incorporating the provision of mortgage finance.
- Treasury – operates the Group's funds management and forex business activities
- Other Group's operations comprise business support activities

The table below analysis the breakdown of segmental assets, liabilities, income and expenses of the Group;

Income statement

	Corporate banking KShs'000	Retail banking KShs'000	Treasury KShs'000	Mortgages KShs'000	Other KShs'000	Total KShs'000
For the year ended 31 December 2011						
Net interest income	7,739,891	9,162,907	3,361,616	3,021,997	-	23,286,411
Net fees and commission income	2,537,184	5,928,360	126,297	137,606	-	8,729,447
Other income	2,369	689,447	3,335,200	48,686	413,085	4,488,787
Operating expenses	(1,132,856)	(9,350,295)	(367,537)	(125,168)	(10,399,415)	(21,375,271)
Profit before tax	9,146,588	6,430,419	6,455,576	3,083,121	(9,986,330)	15,129,374
For the year ended 31 December 2010						
Net interest income	6,103,223	6,243,635	5,134,455	2,164,012	-	19,645,325
Net fees and commission income	1,426,457	4,918,493	17,142	120,333	-	6,482,425
Other income	250,520	156,556	2,775,494	-	18,488	3,201,058
Operating expenses	(1,680,638)	(6,829,001)	(1,023,871)	(685,867)	(9,311,460)	(19,530,837)
Profit before tax	6,099,562	4,489,683	6,903,220	1,598,478	(9,292,972)	9,797,971

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

7. SEGMENT REPORTING (Continued)

Statement of financial position	Corporate banking KShs'000	Retail banking KShs'000	Treasury KShs'000	Mortgages KShs'000	Other KShs'000	Total KShs'000
As at 31 December 2011						
Total Assets	110,361,709	91,784,304	87,813,615	27,444,090	13,312,441	330,716,159
Total Liabilities	123,119,771	115,724,525	27,997,935	9,428,891	10,080,010	286,351,132
Equity	-	-	-	-	44,365,027	44,365,027
	123,119,771	115,724,525	27,997,935	9,428,891	54,445,037	330,716,159
As at 31 December 2010						
Total Assets	78,818,388	79,077,461	56,145,638	21,107,514	16,207,199	251,356,200
Total Liabilities	83,309,194	71,419,022	46,916,876	6,386,526	4,194,811	212,226,429
Equity	-	-	-	-	39,129,771	39,129,771
	83,309,194	71,419,022	46,916,876	6,386,526	43,324,582	251,356,200

Geographical segments

Four of the Group companies, KCB (Tanzania) Limited, KCB Sudan Limited, KCB Bank Uganda Limited and KCB Rwanda SA operate outside the domestic financial market. The table below analyses the geographical segments (per country) in which the Group operates.

Income statement	Kenya KShs'000	Tanzania KShs'000	South Sudan KShs'000	Uganda KShs'000	Rwanda KShs'000	Total KShs'000
As at 31 December 2011						
Net interest income	21,276,762	660,581	348,096	462,067	538,905	23,286,411
Net fees and commission income	6,537,178	373,171	1,275,840	272,201	271,057	8,729,447
Other income	2,775,068	126,226	1,161,205	259,286	167,002	4,488,787
Operating expenses	(16,514,724)	(1,113,398)	(1,921,127)	(966,832)	(859,190)	(21,375,271)
Profit before tax	14,074,284	46,580	864,014	26,722	117,774	15,129,374
As at 31 December 2010						
Net interest income	18,498,381	533,070	247,788	195,343	170,743	19,645,325
Net fees and commission income	5,312,191	221,045	661,237	147,675	140,277	6,482,425
Other income	1,733,182	128,609	1,171,261	106,769	61,237	3,201,058
Operating expenses	(15,489,223)	(993,400)	(1,499,339)	(859,108)	(689,767)	(19,530,837)
Profit before tax	10,054,531	(110,676)	580,947	(409,321)	(317,510)	9,797,971

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

7. SEGMENT REPORTING (Continued)

Geographical Segments (Continued)

Statement of financial position	Kenya KShs'000	Tanzania KShs'000	South Sudan KShs'000	Uganda KShs'000	Rwanda KShs'000	Group Elimination KShs' 000	Total KShs'000
31 December 2011							
Total Assets	283,841,340	11,003,064	31,818,136	10,040,474	9,026,178	(15,013,033)	330,716,159
Total Liabilities	237,332,165	9,699,715	29,753,306	8,268,147	7,571,350	(6,273,551)	286,351,132
Total equity	46,509,175	1,303,349	2,064,830	1,772,327	1,454,828	(8,739,482)	44,365,027
	283,841,340	11,003,064	31,818,136	10,040,474	9,026,178	(15,013,033)	330,716,159
31 December 2010							
Total Assets	224,400,875	11,030,840	15,893,930	6,272,464	7,337,442	(13,579,351)	251,356,200
Total Liabilities	182,149,016	9,937,915	14,343,810	5,803,041	6,496,786	(6,504,139)	212,226,429
Total equity	42,251,859	1,092,925	1,550,120	469,423	840,656	(7,075,212)	39,129,771
	224,400,875	11,030,840	15,893,930	6,272,464	7,337,442	(13,579,351)	251,356,200

8. INTEREST INCOME AND EXPENSE

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Interest income				
Interest on loans and advances	23,612,698	17,663,904	21,293,264	16,162,740
Interest on held to maturity and trading investments	3,742,965	5,259,702	3,516,523	5,178,712
Interest on placements and bank balances	546,989	186,187	371,521	99,810
	27,902,652	23,109,793	25,181,308	21,441,262
Interest expense				
Interest on deposits	3,821,853	3,307,581	3,308,614	2,802,736
Interest on borrowed funds	794,388	156,887	595,932	140,145
	4,616,241	3,464,468	3,904,546	2,942,881
Net interest income	23,286,411	19,645,325	21,276,762	18,498,381
9. FOREIGN EXCHANGE INCOME				
Foreign currency dealings	3,283,453	2,322,141	1,678,296	1,150,880
Translation gains	324,383	453,353	262,291	206,778
	3,607,836	2,775,494	1,940,587	1,357,658
10. DIVIDEND INCOME				
Dividend received from subsidiary company	-	-	-	1,518,063
Available for sale investments	26,157	1,185	26,157	1,185
	26,157	1,185	26,157	1,519,248

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
11. OTHER OPERATING INCOME				
Rent income	95,245	88,583	90,564	84,082
Profit on disposal of property and equipment	238,748	24,139	235,772	7,928
Miscellaneous income	520,801	311,657	477,300	277,820
	854,794	424,379	803,636	369,830
12. NET IMPAIRMENT LOSSES ON FINANCIAL ASSETS				
Additional specific provisions (Note 21b)	2,435,362	1,648,351	2,109,587	1,425,944
Additional collective provisions (Note 21c)	(539,280)	495,969	(637,719)	472,286
Bad debts recovered (Note 21b)	(2,349,039)	(1,026,424)	(2,348,497)	(1,022,819)
	(452,957)	1,117,896	(876,629)	875,411
13. OTHER OPERATING EXPENSES				
Administrative expenses	8,608,561	7,152,733	6,383,417	5,115,911
Personnel costs	10,883,679	9,383,643	9,222,469	8,024,266
Directors' emoluments - As directors	74,900	37,255	35,532	28,376
- As executives	70,692	63,146	70,692	63,146
Depreciation of property and equipment	1,672,850	1,382,540	1,166,348	1,029,436
Amortisation of intangible assets	497,685	375,249	488,098	371,219
Amortisation of prepaid operating lease rentals	861	2,065	826	2,030
Auditors' remuneration	19,000	16,310	11,700	9,980
	21,828,228	18,412,941	17,379,082	14,644,364
Personnel costs:				
Salaries and wages	7,527,919	7,172,777	6,239,924	6,039,143
Medical expenses	376,014	375,212	318,129	252,294
Pension scheme contributions	859,434	455,676	774,859	400,622
Other	2,120,312	1,379,978	1,889,557	1,332,207
	10,883,679	9,383,643	9,222,469	8,024,266

The number of employees of the Group as at 31 December 2011 was 5,571 (31 December 2010 - 5,639).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

14. INCOME TAX

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(a) Income statement				
Current tax	3,998,076	3,647,924	3,908,839	3,560,777
Defferred tax charge/(credit)	64,349	(1,031,246)	248,787	(842,104)
Under provision in the previous years	85,903	3,320	85,903	-
	4,148,328	2,619,998	4,243,529	2,718,673
Accounting profit before tax	15,129,374	9,797,971	14,081,866	11,537,533
Tax calculated at tax rate of 30%	4,538,812	2,939,391	4,224,560	3,461,260
Tax effects on non-taxable/non-deductible items:				
Depreciation on non qualifying assets	101,735	(89,339)	100,900	(90,655)
Provisions	(200,965)	(503,060)	(200,965)	(353,525)
Unrealised exchange gains	(78,687)	(412,175)	(78,687)	(472,177)
Under provisions in previous years	85,903	3,320	85,903	-
Other non deductible items	(298,470)	681,861	111,818	173,770
	4,148,328	2,619,998	4,243,529	2,718,673
(b) Statement of financial position				
At 1 January	(1,826,713)	399,009	(1,750,345)	494,903
Tax paid during the year	5,793,529	1,425,520	5,754,505	1,315,529
Tax charge for the year	(3,998,076)	(3,647,924)	(3,908,839)	(3,560,777)
Translation difference	18,348	2	-	-
Under provision in the previous years	(85,903)	(3,320)	(85,903)	-
At 31 December	(98,815)	(1,826,713)	9,418	(1,750,345)
Comprising:				
Tax recoverable	20,557	11,009	9,418	(1,750,345)
Tax payable	(119,372)	(1,837,722)	-	-
	(98,815)	(1,826,713)	9,418	(1,750,345)

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

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15. EARNINGS PER SHARE

Basic and diluted earnings per share is calculated on the profit attributable to ordinary shareholders of KShs 10,981 million and KShs. 9,838 million for the Group and Bank, respectively (2010: KShs 7,178 million and KShs 8,819 million for the Group and Bank, respectively) and on the weighted average number of ordinary shares during the year of 2,952 Million (2010: 2,597 million shares).

	GROUP		BANK	
	2011 KShs	2010 KShs	2011 KShs	2010 KShs
Diluted earnings per share (KShs.)	3.72	2.76	3.33	3.40

16. DIVIDEND PER SHARE

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 18th May 2012, a final dividend in respect of the year ended 31 December 2011 of KShs. 5,492,180,389 (2010 – KShs.3,687,824,773) is to be proposed. Payment of dividends is subject to withholding tax at the rate of 5% for residents and 10% for non-resident shareholders.

	GROUP AND BANK	
	2011 KShs	2010 KShs
Dividends per share (KShs.)	1.85	1.25

17. CASH AND BALANCES WITH CENTRAL BANKS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Cash on hand	15,697,286	10,009,715	8,582,793	5,777,976
Balances with Central Banks:				
Cash reserve ratio	13,234,839	8,596,748	11,555,840	7,276,616
Other current accounts	13,775,891	8,391,360	-	741,919
	42,708,016	26,997,823	20,138,633	13,796,511

Cash held with Central Banks represent cash ratio and other non-interest earning current accounts. Mandatory cash reserve ratio is not available for use in the Group's day-to-day operations and is based on the value of deposits as adjusted for Central Bank requirements.

18. DUE FROM BANKS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Balances in nostro accounts	11,022,721	2,229,932	9,774,005	1,013,199
Placements with other banks	14,789,363	7,981,076	7,874,875	2,946,764
	25,812,084	10,211,008	17,648,880	3,959,963

The weighted average effective interest rate on balances due from other banks at 31 December 2011 was 27% (2010- 3 %)

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

19. HELD FOR TRADING INVESTMENTS	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Treasury bonds	367,938	847,876	367,938	847,876

Treasury bonds are debt securities issued by the Government of the Republic of Kenya and acquired by the bank for the generation of revenue from short term fluctuations in interest rates. The weighted average effective interest rates on treasury bonds as at 31 December 2011 was 7.8% (31 December 2010 – 9.6 %.)

20. AVAILABLE FOR SALE INVESTMENTS	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Quoted investments	469,743	292,700	469,743	292,700
Unquoted equity investments	4,765	4,765	4,765	4,765
Corporate bonds	1,939,300	2,139,300	1,939,300	2,139,300
Treasury bonds	6,790,693	3,425,723	6,790,693	3,425,723
	9,204,501	5,862,488	9,204,501	5,862,488

21. LOANS AND ADVANCES TO CUSTOMERS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(a) Loans and advances to customers				
Gross loans and advances to customers	206,716,627	158,765,290	186,833,662	147,426,418
Specific provisions for impairment	(6,466,159)	(8,587,097)	(5,724,058)	(8,178,514)
Collective provisions for impairment	(1,525,549)	(2,064,829)	(1,265,617)	(1,903,336)
Loans and advances to customers (net)	198,724,919	148,113,364	179,843,987	137,344,568
(b) Specific provisions for impairment				
At 1 January	8,587,097	8,189,513	8,178,514	7,593,959
Transfer from Savings & Loan	-	-	-	493,834
Provisions made during the year	2,435,362	1,648,351	2,109,587	1,425,944
Interest suspended during the year	598,735	713,052	450,258	618,397
Provisions recovered/no longer required	(2,349,039)	(1,026,424)	(2,348,497)	(1,022,819)
Write downs/write offs during the year	(2,805,996)	(937,395)	(2,665,804)	(930,801)
At 31 December	6,466,159	8,587,097	5,724,058	8,178,514
(c) Collective provisions for impairment				
At 1 January	2,064,829	1,568,860	1,903,336	1,264,858
Transfer from Savings & Loan	-	-	-	166,192
Provisions made during the year	(539,280)	495,969	(637,719)	472,286
At 31 December	1,525,549	2,064,829	1,265,617	1,903,336

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

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21. LOANS AND ADVANCES TO CUSTOMERS (Continued)

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(d) Maturity analysis of gross loans and advances to customers:				
Maturing within 1 month	24,315,451	15,178,819	21,127,485	14,054,677
Maturing after 1 month, but before 3 months	10,742,513	6,350,676	10,275,864	5,314,618
Maturing after 3 months, but within 1 year	17,160,163	13,582,203	14,707,637	11,793,253
Maturing after 1 year, but within 5 years	73,617,715	66,756,226	64,055,939	60,586,837
Maturing after 5 years	80,880,785	56,897,366	76,666,737	55,677,033
	206,716,627	158,765,290	186,833,662	147,426,418
(e) Sectoral analysis of gross loans and advances to customers:				
Private sector and individuals	200,792,505	152,734,650	180,901,865	141,395,778
Government and parastatals	5,924,122	6,030,640	5,931,797	6,030,640
	206,716,627	158,765,290	186,833,662	147,426,418

The weighted average effective interest rates on loans and advances as at 31 December 2011 was 12.7% (2010: 12.5%).

As at 31 December, the aging analysis of past due but not impaired loans and advances is as follows:

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Less than 60 days	11,697,074	9,421,165	10,711,013	8,887,363
Between 60 – 120 days	1,372,589	700,998	1,047,623	524,522
Greater than 120 days	922,798	89,951	-	-
	13,992,461	10,212,114	11,758,636	9,411,885

22. HELD TO MATURITY INVESTMENTS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(a) Treasury bills				
Maturing within 1 month	60,038	2,138,342	-	1,999,241
Maturing between 1-3 months	323,328	4,589,408	-	4,235,056
Maturing between 3-6 months	979,550	2,772,617	-	2,422,388
	1,362,916	9,500,367	-	8,656,685

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

22. HELD TO MATURITY

INVESTMENTS (Continued)

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(b) Treasury bonds				
Maturing between 3-12 months	3,190,924	2,858,938	3,180,722	2,667,285
Maturing between 1-5 years	15,460,537	12,078,802	14,808,217	11,767,338
Maturing after 5 years	16,417,820	18,960,027	16,034,423	18,960,027
	35,069,281	33,897,767	34,023,362	33,394,650
TOTAL GOVERNMENT SECURITIES	36,432,197	43,398,134	34,023,362	42,051,335
Maturing as follows:-				
Maturing within 1 month	60,038	2,138,342	-	1,999,241
Maturing between 1-3 months	323,328	4,589,408	-	4,235,056
Total (maturing within 3 months)	383,366	6,727,750	-	6,234,297
Maturing between 3-12 months	4,170,474	5,631,555	3,180,722	5,089,673
Maturing between 1-5 years	15,460,537	12,078,802	14,808,217	11,767,338
Maturing after 5 years	16,417,820	18,960,027	16,034,423	18,960,027
	36,432,197	43,398,134	34,023,362	42,051,335

Treasury bills and bonds are debt securities issued by the Government of the Republic of Kenya, Government of Uganda, Government of the Republic of Rwanda, and United Republic of Tanzania. The bills and bonds are categorized as amounts held to maturity and carried at amortized cost. The weighted average effective interest rates on treasury bonds and bills as at 31 December 2011, was 7.81 % and 8.6% respectively (31 December 2010 - 9.6 % and 2.8% respectively).

23. OTHER ASSETS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Other receivables	5,524,621	4,260,518	3,878,533	3,817,705
Prepayments	1,183,770	741,771	903,266	368,076
	6,708,391	5,002,289	4,781,799	4,185,781

Other receivables are current and non-interest bearing and are generally between 30 to 90 days terms.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

24. DEFERRED TAX

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
At 1 January	1,126,163	94,917	855,115	(12,225)
Transfer from Savings & Loan	-	-	-	25,236
(Charge)/Credit for the year	(64,349)	1,031,246	(248,787)	842,104
Translation difference	(6,338)	-	-	-
At 31 December	1,055,476	1,126,163	606,328	855,115
The net deferred tax asset is attributable to the following items:				
Depreciation over tax allowances	(246,875)	(209,617)	(102,311)	(181,791)
Provisions	762,436	1,249,464	708,639	1,036,906
Tax losses carried forward	539,915	86,316	-	-
	1,055,476	1,126,163	606,328	855,115
Comprising:				
Deferred tax asset	1,055,476	1,126,284	606,328	855,115
Deferred tax liability	-	(121)	-	-
	1,055,476	1,126,163	606,328	855,115

25. INTANGIBLE ASSETS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
COST				
At 1 January	2,479,362	2,090,206	2,426,108	2,072,445
Transfer from Savings & Loan	-	-	-	17,555
Reclassifications	66,834	-	66,834	-
Additions	581,782	389,156	581,123	336,108
At 31 December	3,127,978	2,479,362	3,074,065	2,426,108
AMORTISATION				
At 1 January	1,110,977	735,728	1,106,741	717,967
Transfer from Savings & Loan	-	-	-	17,555
Reclassifications	2,632	-	2,632	-
Amortisation for the year	497,685	375,249	488,098	371,219
At 31 December	1,611,294	1,110,977	1,597,471	1,106,741
CARRYING AMOUNT				
At 31 December	1,516,684	1,368,385	1,476,594	1,319,367

The intangible assets are in respect of computer software costs.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

26. PROPERTY AND EQUIPMENT

(a) GROUP	Freehold and leasehold premises	Leasehold improvements	Motor vehicles, furniture and equipment	Total
As at 31 December 2011:	KShs'000	KShs'000	KShs'000	KShs'000
COST:				
At 1 January 2011	2,139,907	1,053,727	11,101,657	14,295,291
Additions	15,666	500,512	1,216,008	1,732,186
Reclassification	34,721	-	(101,555)	(66,834)
Disposals	(119,200)	(4,151)	(164,063)	(287,414)
Translation differences	(12,021)	(64,879)	(59,224)	(136,124)
At 31 December 2011	2,059,073	1,485,209	11,992,823	15,537,105
DEPRECIATION				
At 1 January 2011	313,874	236,645	5,473,125	6,023,644
Charge for the year	39,313	292,644	1,340,893	1,672,850
Reclassification	6,041	-	(8,673)	(2,632)
Disposals	(32,550)	(399)	(134,062)	(167,011)
Translation differences	(1,507)	(4,892)	(942)	(7,341)
At 31 December 2011	325,171	523,998	6,670,341	7,519,510
NET BOOK VALUE				
At 31 December 2011	1,733,902	961,211	5,322,482	8,017,595
As at 31 December 2010:				
COST				
At 1 January 2010	2,066,203	502,212	9,932,697	12,501,112
Additions	105,328	551,454	1,246,777	1,903,559
Disposals	(40,212)	-	(85,250)	(125,462)
Translation differences	8,588	61	7,433	16,082
At 31 December 2010	2,139,907	1,053,727	11,101,657	14,295,291
DEPRECIATION				
At 1 January 2010	298,935	118,064	4,337,494	4,754,493
Charge for the year	54,720	124,286	1,203,534	1,382,540
Disposals	(40,212)	-	(67,970)	(108,182)
Translation differences	431	(5,705)	67	(5,207)
At 31 December 2010	313,874	236,645	5,473,125	6,023,644
NET BOOK VALUE				
At 31 December 2010	1,826,033	817,082	5,628,532	8,271,647

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

26. PROPERTY AND EQUIPMENT (Continued)

(b) BANK

As at 31 December 2011

COST

At 1 January 2011

	Freehold and leasehold premises KShs'000	Leasehold improvements KShs'000	Motor vehicles, furniture and equipment KShs'000	Total KShs'000
At 1 January 2011	1,626,457	77,308	9,591,997	11,295,762
Additions	2,000	-	1,073,049	1,075,049
Reclassification	34,721	-	(101,555)	(66,834)
Disposals	(119,200)	-	(140,788)	(259,988)

At 31 December 2011

DEPRECIATION

At 1 January 2011

At 31 December 2011	1,543,978	77,308	10,422,703	12,043,989
At 1 January 2011	271,554	73,491	5,062,432	5,407,477
Charge for the year	15,090	2,330	1,148,928	1,166,348
Reclassification	6,041	-	(8,673)	(2,632)
Disposals	(32,551)	-	(119,419)	(151,970)

At 31 December 2011

NET BOOK VALUE

At 31 December 2011

As at 31 December 2010

COST:

At 1 January 2010

At 31 December 2010	1,626,457	77,308	9,591,997	11,295,762
At 1 January 2010	1,613,769	77,308	8,478,218	10,169,295
Transfer from S&L	-	-	157,566	157,566
Additions	12,688	-	1,024,084	1,036,772
Disposals	-	-	(67,871)	(67,871)

DEPRECIATION

At 1 January 2010

At 31 December 2010	271,554	73,491	5,062,432	5,407,477
At 1 January 2010	256,249	71,789	4,013,264	4,341,302
Transfer from S&L	-	-	104,408	104,408
Charge for the year	15,305	1,702	1,012,429	1,029,436
Disposals	-	-	(67,669)	(67,669)

At 31 December 2010

NET BOOK VALUE

At 31 December 2010

At 31 December 2010	1,354,903	3,817	4,529,565	5,888,285
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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

27. PREPAID OPERATING LEASE RENTALS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
COST				
At 1 January	223,031	223,031	219,574	219,574
Additions	2,769	-	-	-
At 31 December	225,800	223,031	219,574	219,574
AMORTISATION				
At 1 January	77,138	75,073	75,930	73,900
Charge for the year	861	2,065	826	2,030
At 31 December	77,999	77,138	76,756	75,930
NET BOOK VALUE				
At 31 December	147,801	145,893	142,818	143,644

28. INVESTMENT IN SUBSIDIARIES AND ASSOCIATED COMPANIES

		Beneficial ownership	2011 KShs'000	2010 KShs'000
Investments insubsidiaries:				
Incorporated in Kenya:				
Company	Activity	%		
Kenya Commercial Finance Co. Ltd	Dormant	100	150,000	150,000
Savings & Loan Kenya Ltd	Dormant	100	500,000	500,000
KCB Foundation	Corporate social responsibility	-	-	-
Kenya Commercial Bank Nominees Ltd	Nominee	-	-	-
Kencom House Ltd	Shareholders	100	-	-
	Property ownership & management	100	748,645	748,645
Investment in associates:				
United Finance Ltd	Dormant	45	125	125
Incorporated outside Kenya:				
KCB (Tanzania) Ltd	Commercial banking	100	1,795,446	1,570,446
KCB Sudan Ltd	Conventional banking	100	1,025,648	1,025,363
KCB Rwanda SA	Commercial banking	100	1,720,681	1,163,174
KCB Bank Uganda Ltd	Commercial banking	100	2,683,984	1,611,870
			8,624,529	6,769,623

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

29. DUE TO BANKS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Deposits and balances from other banks	14,105,149	11,056,967	11,502,571	10,807,301
Maturing as follows:				
Payable within 1 month	14,105,149	11,056,967	11,502,571	10,807,301

The weighted average effective interest rates on deposits and balances from other banks as at 31 December 2011 was 1.0 % (31 December 2010 - 1.2 %).

30. CUSTOMER DEPOSITS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(a) From government and parastatals:				
Payable within 1 month	43,117,241	43,903,496	42,733,273	42,425,481
Payable after 1 month, but within 3 months	12,139,631	923,819	12,139,329	923,819
Payable after 3 months, but within 1 year	9,552,594	4,202,150	9,552,594	4,202,150
Payable after 1 year, but within 5 years	1,217,376	899,073	962,192	899,073
	66,026,842	49,928,538	65,387,388	48,450,523
(b) From private sector and individuals:				
Payable within 1 month	144,974,969	121,761,351	103,571,209	95,559,214
Payable after 1 month, but within 3 months	20,783,547	4,867,084	17,507,259	2,717,304
Payable after 3 months, but within 1 year	21,420,820	15,358,085	18,102,455	11,402,115
Payable after 1 year, but within 5 years	6,102,671	5,059,593	5,605,203	5,059,525
	193,282,007	147,046,113	144,786,126	114,738,158
Total other customer deposits	259,308,849	196,974,651	210,173,514	163,188,681
Maturing as follows:				
Payable within 1 month	188,092,210	165,664,847	146,304,482	137,984,695
Payable after 1 month but within 3 months	32,923,178	5,790,903	29,646,588	3,641,123
Payable after 3 months but within 1 year	30,973,414	19,560,235	27,655,049	15,604,265
Payable after 1 year but within 5 years	7,320,047	5,958,666	6,567,395	5,958,598
	259,308,849	196,974,651	210,173,514	163,188,681

The weighted average effective interest rates on interest bearing customer deposits as at 31 December 2011 was 1.6% (31 December 2010 – 1.1%).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

31. OTHER LIABILITIES

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Bills payable	731,796	706,405	671,829	691,405
Accrued expenses	403,972	329,046	221,180	153,942
Defined pension benefit obligation	266,000	-	266,000	-
Other payables	2,890,994	1,321,517	451,194	918,385
	4,292,762	2,356,968	1,610,203	1,763,732

32. RELATED PARTY TRANSACTIONS

A number of transactions are entered into with related parties in the normal course of business. These include loans, deposits and foreign currency transactions. The volumes of related party transactions, outstanding balances at the end of the year and the related expenses and income for the year are as follows:

(a) Balances due from group companies

	2011 KShs'000	2010 KShs'000
KCB (Tanzania) Limited	408,730	993,964
	408,730	993,964

(b) Balances due to group companies

	2011 KShs'000	2010 KShs'000
Savings and Loan Kenya Limited	499,900	499,900
Kencom House Limited	472,696	482,672
Kenya Commercial Finance Company Limited	112,160	112,160
KCB Bank Uganda Limited	120,190	66,243
KCB Foundation	77,920	79,834
KCB Rwanda SA	611,036	1,941,904
KCB Sudan Limited	4,034,435	2,449,303
Total balances due to group companies	5,928,337	5,632,016
	5,519,607	4,638,052

Balances due from/to group companies are non interest bearing, are current and are generally on 30-90 day term. The balances relate to transactions entered into with the subsidiary companies at arm's length in the ordinary course of business.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

32. RELATED PARTY

TRANSACTIONS (Continued)

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(c) Shareholders, directors and key management personnel				
(i) Loans				
Government of Kenya	824,151	241,910	824,151	241,910
Directors	3,736,431	3,971,283	3,719,141	3,956,958
Senior management	859,511	245,766	737,738	244,459
Other employees	5,730,895	4,744,183	5,155,987	4,711,595
	11,150,988	9,203,142	10,437,017	9,154,922
Movement in loans to directors and senior management				
At 1 January	4,217,049	3,723,655	4,201,417	3,707,936
Loans issued during the year	1,249,091	1,203,161	896,871	1,126,836
Loans repayments during the year	(870,198)	(709,767)	(641,409)	(633,355)
At 31 December	4,595,942	4,217,049	4,456,879	4,201,417
Interest income earned	676,923	773,407	640,003	770,543
(ii) Deposits				
Government of Kenya	36,850,507	34,754,485	36,314,209	34,754,485
Directors	1,607,262	1,242,652	1,601,587	1,224,321
Senior management	449,362	483,106	440,743	483,106
Other employees	253,154	109,108	110,186	88,135
	39,160,285	36,589,351	38,466,725	36,550,047
Movement in deposits by directors and senior management:				
At 1 January	1,725,758	1,507,312	1,707,427	1,448,956
Deposits received during the year	1,872,858	2,459,079	1,704,173	2,427,641
Deposits withdrawn during the year	(1,541,992)	(2,240,633)	(1,369,270)	(2,169,170)
At 31 December	2,056,624	1,725,758	2,042,330	1,707,427
Interest expense	145,644	97,392	143,961	95,999
(iii) Senior management personnel compensation (Included under personnel costs - Note 13)				
Short term employee benefits	516,744	479,949	374,147	242,586
Post employment pension and medical benefits	28,795	9,462	19,530	6,401
	545,539	489,411	393,677	248,987

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

33. LONG TERM DEBT

	GROUP AND BANK	
	2011 KShs'000	2010 KShs'000
Long term debt	8,525,000	-

During the year the bank obtained a 7 year term loan from International Finance Corporation (IFC) of USD 100 Million. The effective interest rate as at 31 December 2011 was 2.3%.

34. SHARE CAPITAL

	2011 KShs'000	2010 KShs'000
Authorised:-		
3,500,000,000 (2010: 3,500,000,000) ordinary shares of KShs.1 each	3,500,000	3,500,000
Issued and fully paid:-		
2,968,746,156 (2010: 2,950,259,818) ordinary shares of KShs.1 each	2,968,746	2,950,260

During the year the bank offered 18,486,338 shares through Employee Shares Options (ESOP) at KShs. 18.62 per share. The movement in share capital during the year was as follows:

	2011 KShs'000	2010 KShs'000
At January		
Rights issue	-	732,482
Employee share option exercised	18,486	-
As at 31 December	2,968,746	2,950,260

The top ten largest shareholders as at 31 December 2011 were:

Shareholder	No. of Shares	%
Permanent Secretary to the Treasury of Kenya	523,600,000	17.64
National Social Security Fund	225,230,355	7.59
Standard Chartered Nominees A/C 9688	72,490,723	2.44
Standard Chartered Nominees Non Resident A/C 9318	57,640,058	1.94
Standard Chartered Nominees Non Resident A/C 9011	54,875,100	1.85
CFC Stanbic Nominees LTD A/C R48701	53,775,626	1.81
Standard Chartered Nominees A/C 9687	42,570,686	1.43
Standard Chartered Nominees A/C 9230	31,986,787	1.08
Kanaksinh Karsandas & Sandip Kanaksinh Babla	28,991,920	0.98
Old Mutual Life Assurance Company Limited	23,182,044	0.78
Total shares	1,114,343,299	37.54

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

34. SHARE CAPITAL (Continued)

The distribution of shareholders as at 31 December 2011 was as follows:

Share range	No. of shareholders	Shares held	%
1 to 5000	131,721	227,252,630	7.65
5,001-50,000	31,611	337,981,787	11.38
50,001-100,000	964	66,171,093	2.23
100,001-1,000,000	914	258,368,480	8.71
1,000,001-10,000,000	206	644,947,903	21.72
10,000,001 and above	32	1,434,024,263	48.31
	165,448	2,968,746,156	100.00

35. RESERVES

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Retained earnings	17,721,580	13,953,178	18,276,521	15,388,072
Share premium	18,891,221	18,565,504	18,891,221	18,565,504
Available-for-sale reserve	(1,983,146)	225,356	(1,983,146)	225,356
Statutory credit risk reserve	1,866,093	145,629	1,517,136	59,428
Translation reserve	(591,647)	(397,981)	-	-
	35,904,101	32,491,686	36,701,732	34,238,360

Share premium arises from issue of shares at a price higher than the par value of the shares

The available-for-sale reserve arises from marking to market of investment securities classified under available-for-sale category.

Statutory credit risk reserve represents an amount set aside to cover additional provision for loan losses required to comply with the requirements of Central Banks Prudential guidelines. This amount is not available for distribution.

The translation reserve arises from translation of the net investment in foreign subsidiaries to Kenya Shillings.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

36. NOTES TO THE STATEMENT OF CASH FLOWS

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
(a) Cash flows from operating activities				
This has been derived as follows:-				
Profit before tax	15,129,374	9,797,971	14,081,866	11,537,533
Adjustments for:				
Depreciation of property and equipment	1,672,850	1,382,540	1,166,348	1,029,436
Amortisation of prepaid operating lease rentals	861	2,065	826	2,030
Amortisation of intangible assets	497,685	375,249	488,098	371,219
Profit on disposal of available for sale investments	-	(137,110)	-	(137,110)
Profit/loss on disposal of property and equipment	(238,748)	(24,139)	(235,772)	(7,928)
Operating profit before movements in operating assets and liabilities	17,062,022	11,396,576	15,501,366	12,795,180
Cash reserve ratio	(4,638,090)	(1,937,431)	(4,279,224)	(1,294,440)
Available for sale investments	(5,550,515)	(3,926,653)	(5,550,515)	(3,926,653)
Held to maturity investments	621,553	(17,891,679)	1,793,676	(17,684,870)
Loans and advances	(50,611,555)	(25,454,282)	(42,499,419)	(38,594,950)
Balances due from group companies	-	-	881,555	9,821,927
Other assets	(1,706,102)	1,830,399	(596,018)	1,783,599
Other customer deposits	62,334,198	33,945,301	46,984,833	24,735,950
Other liabilities	1,935,794	(30,193)	(153,529)	(447,819)
	19,447,305	(2,067,962)	12,082,725	(12,812,076)
(b) Analysis of cash and cash equivalents				
Balances with Central Banks	13,775,891	8,391,360	-	741,919
Cash on hand	15,697,286	10,009,715	8,582,793	5,777,976
Held to maturity investments	383,366	6,727,750	-	6,234,297
Held for trading investments	367,938	847,876	367,938	847,876
Due from banks	25,812,084	10,211,008	17,648,880	3,959,963
Due to banks	(14,105,149)	(11,056,967)	(11,502,571)	(10,807,301)
	41,931,416	25,130,742	15,097,040	6,754,730

For the purpose of the statement of cash flows, cash and cash equivalents comprise balances with less than three months maturity from the date of acquisition. Cash and cash equivalents excludes the cash reserve requirement held with the Central Banks.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

37. COMMITMENTS

To meet the financial needs of the customers, the Group enters into various irrevocable commitments. Even though these obligations may not be recognized on the statement of financial position, they do contain credit risk and are therefore part of the overall risk of the Group.

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
Capital commitments contracted for at year end	170,164	176,569	132,777	130,073
Loans committed but not disbursed at year end	44,586,173	32,447,570	43,639,631	31,750,911
Foreign currency commitments	184,536	(44,169)	97,759	(44,169)

Commitments to extend credit represent contractual commitments to make loans and other credit facilities. Commitments generally have fixed expiry dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.

	GROUP		BANK	
	2011 KShs'000	2010 KShs'000	2011 KShs'000	2010 KShs'000
38. CONTINGENT LIABILITIES Letters of credit, acceptances, guarantees, indemnities and other engagements entered into on behalf of customers at year end	87,424,335	72,429,394	84,557,085	69,532,289

Letters of credit, guarantees and acceptances commit the Bank and its subsidiary companies to make payments on behalf of the customers in the event of a specific act, generally relating to the import and export of goods. Guarantees and letters of credit carry the same credit risk as loans.

In addition to this, litigation is a common occurrence in the banking industry due to the nature of the business. The Bank and its subsidiary companies have established protocol for dealing with such legal claims. Once professional advice has been obtained and the amount of damages reasonably estimated, the Group makes adjustments to account for any adverse effects which the claim may have on its financial standing.

At year end, the Group had several unresolved legal and tax claims. However, the Group believes, based on the information currently available, that the ultimate resolution of these legal proceedings and tax claims would not likely have a material effect on its operations.

39. RETIREMENT BENEFIT OBLIGATIONS

(a) KCB Pension Fund and Staff Retirement Benefit Scheme

The Group operates both defined contribution scheme and defined benefit scheme for all full time permanent employees.

The benefits provided by the defined benefit scheme are based on a formula taking into account years of service and remuneration levels, whilst the benefits provided by the defined contribution scheme are determined by accumulated contributions and returns on investments.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

39. RETIREMENT BENEFIT OBLIGATIONS (Continued)

Both schemes are governed by the Retirement Benefits Act, 1997. This requires that an actuarial valuation be carried out at least every 3 years for the defined benefit scheme. An actuarial valuation of the Defined Benefit Scheme was done by the actuary as at 31 December 2009 and confirmed that the assets held by the scheme were not sufficient to cover the relevant liabilities accrued at that date. The results of the valuation showed that there is a past service actuarial deficit of KShs. 266 million. In the opinion of the actuary, the assets of the scheme together with the future contributions payable by members in accordance with the regulations should be sufficient to provide the future benefits payable under the scheme provided that the sponsor increases the contribution rate from the current 10.8% to 16.7% of the total pensionable salaries of the members in service. The accelerated contribution at 18% commenced on 1 January 2011.

The amount included in the statement of financial position arising from the Group's obligation in respect of the defined benefit scheme is as follows:

Scheme assets and liabilities

	2011 KShs. 000
Fair value of plan assets	6,872,000
Present value of fund obligations	6,964,000
Deficit	92,000
Unrecognized actuarial gain	174,000
Net retirement benefit liability	266,000
Movement in plan assets	
At 1st January	7,671,000
Expected return on assets	738,000
Employer contributions	127,000
Actuarial gains	(964,000)
Benefits paid	(700,000)
At 31st December	6,872,000
Movement in present value of the retirement benefit obligations	
At 1st January	7,023,000
Current service cost (net of employer contributions)	129,000
Interest cost	674,000
Actuarial gains/(losses)	(287,000)
Benefits paid	(700,000)
Past service cost	125,000
At 31st December	6,964,000

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2011

39. RETIREMENT BENEFIT OBLIGATIONS (Continued)

Historical information

	2011 KShs. 000	2010 KShs. 000	2009 KShs. 000	2008 KShs. 000	2007 KShs. 000
Fair value of plan assets	6,872,000	7,671,000	6,769,000	8,461,100	8,461,100
Present value of benefits	6,964,000	7,023,000	6,780,000	8,925,000	8,925,000
Fund deficit/(surplus)	92,000	(648,000)	11,000	463,900	463,900

The deficit has been accrued in the 2011 financial statements.

The principal actuarial assumptions used are as follows;

Rate of interest	13.5%
Rate of salary escalation	10.0%
Rate of pension increase	Nil

40. OPERATING LEASE COMMITMENTS

Operating lease commitments - Group as lessee

Non-cancellable operating lease rentals are payable as follows:

	2011 KShs'000	2010 KShs'000
Within 1 year	303,704	-
After 1 year but less than 5 years	1,109,068	726,341
After 5 years	422,645	105,888
	1,835,417	832,229

Operating leases – Group as lessor

	2011 KShs. 000	2010 KShs. 000
Within 1 year	52,336	-
After 1 year but less than 5 years	122,454	60,233
After 5 years	17,146	5,246
	191,936	65,479

The Group leases a number of branch and office premises under operating leases. The leases typically run for a year up to ten years, with an option to renew the lease upon expiry. Lease rentals are increased accordingly to reflect market rentals.

PROXY FORM

THE SECRETARY

KENYA COMMERCIAL BANK LTD
8TH FLOOR, KENCOM HOUSE, MOI AVENUE
P.O. BOX 48400-00100 NAIROBI KENYA

I/We _____

ID/Passport No _____

Shares A/C No/CDS A/C No _____

of P.O. Box _____

Being a Member/Members of the above named company hereby appoint _____

ID/Passport No _____

of P.O. Box _____

or failing him the duly appointed Chairman of the meeting to be my/our proxy, to vote on my/our behalf at the 41st Annual General Meeting of the Company to be held on 18th May 2012 at 11:00 a.m or at any adjournment thereof.

Signed _____ this day of _____ 2012

Signature (s)

Note:

1. If a member is unable to attend personally this Form of Proxy should be completed and returned to reach the Company's Registered Office not later than 11.00 a.m. on Wednesday, 16th May 2012 i.e. 48 hours before the time for holding the meeting.
2. A person appointed to act as a proxy need not be a member of the Company.
3. In case of a member being a corporate body, the Proxy Form must be under its Common Seal or under the hand of the officer or attorney duly authorized in writing.



FOMU YA UWAKILISHI

KATIBU

BENKI YA KENYA COMMERCIAL LTD
GOROFA YA NANE,
JUMBA LA KENCOM, MOI AVENUE
S.L.P. 48400-00100 NAIROBI KENYA

Mimi/Sisi _____

Wa kitambulisho/Pasipoti Nambari _____

Hisa A/C No/CDS A/C No _____

wa S.L.P. _____

Nikiwa mwanachama/Wanachama wa kampuni iliyotajwa hapo juu namteua _____

wa kitambulisho/pasipoti nambari _____

wa S.L.P. _____

na akikosa yeye, namteua/tunamteu Mwenyekiti wa mkutano kama mwakilishi wangu/wetu, kupiga kura kwa niaba yangu/ yetu kwenye Mkutano Mkuu wa 41 wa Kampuni utakaofanyika tarehe 18, Mei 2012 saa tano za asubuhi ama siku yoyote ile endapo mkutano huo utaahirishwa.

Imetiwa saini _____ siku ya _____ 2012

Saini

Kumbuka: Iwapo Mwanachama ni Shirika, Fomu ya Uwakilishi ni lazima iwe na muhuri wake au seal iwe na afisa au wakili aliyeidhinishwa kwa maandishi. Si lazima mwakilishi awe Mwanachama wa Kampuni.

Fomu ya uwakilishi ni lazima ifike kwa Msajili tarehe 16 Mei 2012 saa tano za asubuhi, yaani masaa 48 kabla ya mkutano.

