

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES

ANNUAL REPORT

AND

FINANCIAL STATEMENTS

FOR THE YEAR ENDED

31 DECEMBER 2019

✓

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
ANNUAL REPORT AND CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2019

CONTENTS	PAGE
Directors and Statutory Information	1
Report of the Directors	2 - 3
Statement of Directors' Responsibilities	4
Report of the Independent Auditors	5 - 6
Financial Statements:	
Consolidated Statement of Profit or Loss and Other Comprehensive Income	7
Company Statement of Profit or Loss and Other Comprehensive Income	8
Consolidated Statement of Financial Position	9
Company Statement of Financial Position	10
Consolidated Statement of Changes in Equity	11 - 12
Company Statement of Changes in Equity	13
Consolidated Statement of Cash Flows	14 - 15
Company Statement of Cash Flows	16
Notes to the Financial Statements	17 - 87

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
DIRECTORS AND STATUTORY INFORMATION
FOR THE YEAR ENDED 31 DECEMBER 2019

DIRECTORS

NAME		APPOINTMENT	RESIGNATION
Ms. Rose Mwendu	Director	01/07/2015	Current
Mr. Wellington Otiende	Director	05/06/2019	Current
Mr. Lewis Rwinu	Director	18/03/2017	Current
Mr. Kenneth Wapakala	Director	18/03/2017	Current
Mrs. Teresa Mutegi	Director	11/01/2015	5 June 2019
Mrs. Roseline Ochieng	Director	01/07/2015	5 June 2019
Mr. James M Oirere	Director	01/07/2015	5 June 2019
Mr. Joel Gachari	Director	20/02/2016	5 June 2019

SECRETARY

Brenda Kiberenge
mnh@mwalinational.coop
Mwalimu Towers
Upperhill Hill, Hill Lane Off Mara Road, Nairobi
P.O.Box 62641
00200 Nairobi City Square

PRINCIPAL BANKERS

Spire Bank Limited
Mwalimu Towers
Upper Hill - Hill lane, Off Mara Road
P.O. Box 52467-00200
Nairobi, Kenya

REGISTERED OFFICE

LR No. 209/5459
Mwalimu Towers
Upper Hill, Hill Lane, Off Mara Road, Nairobi
P.O. Box 62641
00200 Nairobi City Square

LEGAL ADVISORS

Mose, Mose & Millimo Advocates
3rd floor, Comcraft House
Haile Sellasie Avenue
P.O. Box 9403
00200 Nairobi City Square

AUDITORS

Ernst & Young LLP
Certified Public Accountants
Kenya-Re Towers
Upper hill, Off Ragati Road
P.O. Box 44286
00100 Nairobi GPO

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2019

The directors submit their report together with the audited financial statements for the year ended 31 December 2019.

1. INCORPORATION

The company is domiciled in Kenya where it is incorporated as a private company limited by shares under the Kenyan Companies Act, 2015. The address of the registered office is set out on page 1.

2. DIRECTORATE

The directors who held office during the year and to the date of this report are set out on page 1.

3. PRINCIPAL ACTIVITIES

The principal activities of the company is to acquire and hold investments on behalf of Mwalimu National Savings and Credit Co-operative Society Limited.

Mwalimu National Holdings Limited is the holding company of Equatorial Commercial Holdings Limited and Mwalimu Asset Management Limited. The company provides administrative and support services to support efficient operation of the group.

4. RECOMMENDED DIVIDEND

The directors do not recommend the declaration of a dividend for the year (2018: KShs nil).

5. Business review

The 2019 results were impressively better than previous period with operating losses before tax returning a 59% improvement over the previous period.

Interest income

The declining asset base (loans) has had the effect of negatively affecting growth in interest income and as a result our interest income is 29% lower year on year (KShs 517 million). The asset base decline results from the low loan origination occasioned by underfunding.

Interest expense

Interest expense decreased marginally by KShs. 280 million.

Other income

Other income recorded a notable improvement in 2019 of 80% to KShs 410 million.

Operating costs

The normal operational costs show 13% increase the slight increase was due to inflation and was reflecting the management strategic reduction on overall operational costs.

Impairments

The impairment charge decreased by more than 81 % year on year attributed to the fact that the group cautiously chose not to lend. It is also worthwhile to mention that, collections and settlements from the NPL book also resulted to impairments write back.

Balance Sheet Developments

Balance sheet contracted by 17% on a year on year basis primarily due to high loan maturities and accumulated losses.

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
REPORT OF THE DIRECTORS (Continued)
FOR THE YEAR ENDED 31 DECEMBER 2019

6. Business review (continued)

The key balance sheet movements were:

Assets

- Net loans and advances declined due to high loan maturities in addition to liquidation of cash covered facilities to KShs 3.3 Billion (2018: KShs 4.4 Billion). Asset origination is still a challenge due to under capitalization.
- Decrease in investments securities due to maturity of Financial assets at amortized cost with a face value of KShs 500 million.
- Decrease in cash and cash equivalent as a result of deposit liquidation during the year to KShs 351 million (2018: KShs 985 million).
- Decrease in inventory property held for sale due to write down to net realisable value by KShs 328 million.
- Finalisation of disposal of associate in Fidelity shield Insurance Company Ltd of KShs 266.9 million and finalization of Equatorial investment Bank of KShs 16.9 million

Liabilities

- Decrease in Equity attributed to the losses in 2019 of KShs.1.1 Billion.
- Decrease in borrowed funds attributed to maturity of Tier 2 capital (KShs.400 M) and repayment of reverse repo following maturity of financial assets at amortizes cost (bonds) during the year with a face value of KShs 500 Million.
- Decrease in deposit owing to deposit flight by KShs 2.3 Billion.

The focus for the coming financial year and the main determinants of its outcome will be:

- Resumption of asset growth with emphasis on credit union business.
- Improved deposit mobilization that is now yielding results
- Continued recoveries on assets.
- Strengthen the subsidiaries to attract more business in the market and improved operational efficiency.

The cost base continues to be reduced through a business process reengineering which should translate into a near zero-annual increase.

7. STATEMENT AS TO DISCLOSURE TO THE COMPANY'S AUDITOR


With respect to each director at the time this report was approved:

- a) there is, so far as the person is aware, no relevant audit information of which the company's auditor is unaware; and
- b) the person has taken all the steps that the person ought to have taken as a director so as to be aware of any relevant audit information and to establish that the company's auditor is aware of that information.

8. TERMS OF APPOINTMENT OF THE AUDITOR

Ernst & Young LLP retires by rotation. The directors monitor the effectiveness, objectivity and independence of the auditor. The directors also approve the annual audit engagement contract which sets out the terms of the auditor's appointment and the related fees. The agreed auditor's remuneration of KShs 5,773,000 has been charged to profit or loss in the year

By order of the Board


.....
Company Secretary *Brenda Kibereffe*

30 June
.....2020

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
STATEMENT OF DIRECTORS' RESPONSIBILITIES
FOR THE YEAR ENDED 31 DECEMBER 2019

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

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

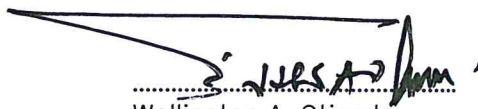
- (i) designing, implementing and maintaining such internal control as they determine necessary to enable the presentation of financial statements that are free from material misstatement, whether due to fraud or error;
- (ii) selecting suitable accounting policies and applying them consistently; and
- (iii) making accounting estimates and judgements that are reasonable in the circumstances.

As disclosed in note 37 to the financial statements, the directors acknowledge the existence of a material uncertainty that may cast significant doubt on the ability of the Group's and company's to continue as a going concern but are of the view that the Group and the company have the resources to continue in business in the foreseeable future and that the realization of assets and settlement of liabilities will occur in the ordinary course of business.

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

Approved by the board of directors on 30th June 2020 and signed on its behalf by:


.....
Rose M. Mutisya
Chairperson


.....
Wellington A. Otiende
Director



Ernst & Young LLP
Certified Public Accountants
Kenya Re Towers
Upper Hill
Off Ragati Road
P.O. Box 44286 - 00100
Nairobi GPO, Kenya

Tel: +254 20 2886000
Email: info@ke.ey.com
www.ey.com
LLP/2015/52

REPORT OF THE INDEPENDENT AUDITOR
TO THE SHAREHOLDERS OF
MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES

REPORT ON THE AUDIT OF THE CONSOLIDATED AND SEPARATE FINANCIAL STATEMENTS

Opinion

We have audited the consolidated and separate financial statement of Mwalimu National Holdings Limited and its subsidiaries (the Group) set out on pages 7 to 87, which comprise the consolidated and separate statement of financial position as at 31 December 2019, and the consolidated and separate statement of profit or loss and other comprehensive income, consolidated and separate statement of changes in equity and consolidated and separate statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of Mwalimu National Holdings Limited as at 31 December 2019, and its consolidated and separate financial performance and consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) and the requirements of the Kenyan Companies Act, 2015.

Basis for opinion

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

Other Information

The directors are responsible for the other information. The other information comprises the report of the directors and statement of directors' responsibility as required by the Kenyan Companies Act, 2015. The other information does not include the consolidated and separate financial statements and our auditor's report thereon.

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

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

Responsibilities of the Directors for the Consolidated and Separate Financial Statements

The directors are responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act, 2015, and for such internal control as the directors determine is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

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

The directors are responsible for overseeing the group's and company's financial reporting processes.



Building a better
working world

Auditor's Responsibilities for the Audit of the Consolidated and Separate Financial Statements

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

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

- Identify and assess the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the group's and company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the group's and company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated and separate financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the group and company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and whether the consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated and separate financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

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

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

REPORT ON OTHER MATTERS PRESCRIBED BY THE KENYAN COMPANIES ACT, 2015

In our opinion, the information given in the report of the directors on page 2 and 3 is consistent with the consolidated and separate financial statements.

The Engagement Partner responsible for the audit resulting in this independent auditors' report is CPA Herbert Chiveli Wasike - Practicing number, 1485.


Nairobi, Kenya
24/11/2020

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
REVENUE			
Interest income on loans and advance	7	517,113	730,775
Interest expense	8	<u>(841,266)</u>	<u>(1,120,889)</u>
Net interest income		(324,153)	(390,114)
Other income	9	410,207	228,227
EXPENSES			
Administrative expenses	10	(1,304,595)	(1,545,109)
Impairment reversals on loans and advances	11	<u>87,066</u>	<u>467,465</u>
Net operating loss before tax		(1,131,475)	(1,239,531)
Income tax expense	12	<u>(29,703)</u>	<u>(1,608,700)</u>
LOSS FOR THE YEAR		<u>(1,161,178)</u>	<u>(2,848,231)</u>
Other comprehensive income		-	-
Total comprehensive income		<u>(1,161,178)</u>	<u>(2,848,231)</u>
Loss for the year attributable to:			
Owners of the company		(1,080,204)	(2,298,131)
Non-controlling interest	33	<u>(80,974)</u>	<u>(550,100)</u>
		<u>(1,161,178)</u>	<u>(2,848,231)</u>
Total comprehensive income for the year attributable to:			
Owners of the company		(1,080,204)	(2,298,131)
Non-controlling interest	33	<u>(80,974)</u>	<u>(550,100)</u>
		<u>(1,161,178)</u>	<u>(2,848,231)</u>

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
 COMPANY STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
 FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
REVENUE			
Interest income on loans and advances	7	301	607
Interest expense	8	<u>-</u>	<u>-</u>
Net interest income		301	607
EXPENSES			
Administrative expenses	10	(2,653)	(3,379)
Increase in impairment provision	11	<u>167</u>	<u>(13)</u>
Net operating loss before tax		(2,185)	(2,785)
Income tax credit	12	<u>1,169</u>	<u>832</u>
LOSS FOR THE YEAR		<u>(1,016)</u>	<u>(1,953)</u>
Other comprehensive income		<u>-</u>	<u>-</u>
TOTAL COMPREHENSIVE INCOME		<u>(1,016)</u>	<u>(1,953)</u>


MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
ASSETS			
Cash and bank balances	13	168,302	410,440
Placements with banking institutions	14	183,089	574,883
Property inventory - ready for sale	15	3,258,356	3,587,105
Land inventory	16	275,077	313,334
Other receivables	17	779,940	619,793
Tax recoverable	12	14,378	15,407
Financial assets at amortised cost	19	2,065,044	2,620,985
Loans and advances to customers	20	3,311,899	4,442,338
Deferred tax asset	21	-	12,957
Investment in associate	22	-	283,943
Intangible assets	24	176,164	44,866
Investment property	25	297,500	280,000
Property and equipment	26	1,210,552	1,397,655
Right of use asset	36	<u>370,906</u>	<u>-</u>
TOTAL ASSETS		<u>12,111,207</u>	<u>14,603,706</u>
EQUITY AND LIABILITIES			
Liabilities			
Deposits from banking institutions	27	1,888,527	2,805,453
Customer and members' deposits	28	4,399,660	6,782,212
Loans and borrowings	29	608,108	1,423,207
Deferred tax liability	21	26,925	-
Other liabilities	30	1,125,597	1,003,780
Amount due to related parties	18	8,890,024	6,858,155
Lease liability	36	<u>383,892</u>	<u>-</u>
Total liabilities		<u>17,322,733</u>	<u>18,872,807</u>
Equity			
Share capital	31	1,210,000	1,210,000
Reserves	32	<u>(6,068,003)</u>	<u>(5,206,553)</u>
Equity attributable to the owners of the company		(4,858,003)	(3,996,553)
Non-controlling interest	33	<u>(353,523)</u>	<u>(272,548)</u>
Total equity		<u>(5,211,526)</u>	<u>(4,269,101)</u>
TOTAL EQUITY AND LIABILITIES		<u>12,111,207</u>	<u>14,603,706</u>

The financial statements were approved by the Board of Directors on 30th June 2020 and were signed on its behalf by:



Rose M. Mutisya
Chairperson



Wellington A. Otiende
Director


MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
 COMPANY STATEMENT OF FINANCIAL POSITION
 AS AT 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
ASSETS			
Cash and bank balances	13	17	1,102
Placements with banking institutions	14	-	4,872
Other assets	17	41,596	42,071
Tax recoverable	12	1,673	1,673
Deferred tax asset	21	5,038	3,869
Investment in subsidiaries	23	<u>4,875,281</u>	<u>3,925,281</u>
TOTAL ASSETS		<u>4,923,605</u>	<u>3,978,868</u>
LIABILITIES AND EQUITY			
LIABILITIES			
Amounts due to related parties	18	3,533,925	2,587,594
Other liabilities	30	<u>265,622</u>	<u>266,200</u>
TOTAL LIABILITIES		<u>3,799,547</u>	<u>2,853,794</u>
EQUITY			
Share capital	31	1,210,000	1,210,000
Accumulated losses	32	<u>(85,942)</u>	<u>(84,926)</u>
TOTAL EQUITY		<u>1,124,058</u>	<u>1,125,074</u>
TOTAL LIABILITIES AND EQUITY		<u>4,923,605</u>	<u>3,978,868</u>

The financial statements were approved by the Board of Directors on 30th June 2020 and signed on its behalf by:



 Rose M. Mutisya
 Chairperson



 Wellington A. Otiende
 Director

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2019

	Share Capital KShs '000	Statutory Reserves KShs '000	Accumulated losses KShs '000	Total KShs '000	Non- controlling interest KShs '000	Total KShs '000
At January 2019	1,210,000	420,123	(5,626,676)	(3,996,553)	(272,548)	(4,269,101)
Loss for the year	-	-	(1,080,204)	(1,080,204)	(80,974)	(1,161,178)
Other comprehensive Income	-	-	-	-	-	-
Total comprehensive Income	-	-	(1,080,204)	(1,080,204)	(80,974)	(1,161,178)
Transfer from statutory credit risk reserve	-	218,755	-	218,755	-	218,755
At 31 December 2019	<u>1,210,000</u>	<u>638,877</u>	<u>(6,706,880)</u>	<u>(4,858,003)</u>	<u>(353,523)</u>	<u>(5,211,526)</u>

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018

	Share Capital KShs '000	Statutory Reserves KShs '000	Accumulated Losses KShs '000	Total KShs '000	Non- controlling interest KShs '000	Total KShs '000
At 1 January 2018	1,210,000	(44,220)	(2,861,401)	(1,695,621)	313,789	(1,381,832)
* Impact of adopting IFRS 9	-	-	(2,801)	(2,801)	-	(2,801)
Impact of adopting IFRS - Minority share	-	-	-	-	(36,237)	(36,237)
Restated opening balance under IFRS 9	1,210,000	(44,220)	(2,864,202)	(1,698,422)	277,522	(1,420,870)
Loss for the year	-	-	(2,298,131)	(2,298,131)	(500,100)	(2,848,231)
Other comprehensive Income	-	-	-	-	-	-
Total comprehensive Income	-	-	(2,298,131)	(2,298,131)	(500,100)	(2,848,231)
Transfer from statutory credit risk reserve	-	464,343	(464,343)	-	-	-
Balance as at 31 December 2018	1,210,000	420,123	(5,626,676)	(3,996,553)	(272,548)	(4,269,101)

*The group applied a new accounting policy on adopting IFRS 9 prospectively, with an initial application date of 1 January 2018. The group has not restated the comparative information, which continues to be reported under IAS 39. Differences arising from the change in accounting policy of IFRS 9 have been recognised directly in accumulated losses and are disclosed in Note 3 (r).

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
 COMPANY STATEMENT OF CHANGES IN EQUITY
 FOR THE YEAR ENDED 31 DECEMBER 2019

	Share capital KShs '000	Accumulated losses KShs '000	Total KShs '000
2019			
At 1 January 2019	1,210,000	(84,926)	1,125,074
Loss for the year	-	(1,016)	(1,016)
At 31 December 2019	<u>1,210,000</u>	<u>(85,942)</u>	<u>1,124,058</u>
2018			
At 1 January 2018	1,210,000	(81,276)	1,128,724
*Impact of adopting IFRS 9	-	(1,697)	(1,697)
Restated balance under IFRS 9	<u>1,210,000</u>	<u>(82,973)</u>	<u>1,127,027</u>
Loss for the year	-	(1,953)	(1,953)
At 31 December 2018	<u>1,210,000</u>	<u>(84,926)</u>	<u>1,125,074</u>

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Loss before taxation		(1,131,475)	(1,239,531)
Write down of property inventory to net realisable value	15	328,749	71,456
Decrease/(increase) in impairment of loans and advances	11	87,066	467,466
Gain on disposal of associate	22	(63,005)	-
Amortisation of intangible assets	24	40,882	28,116
Write off of intangible assets	24	-	29
Fair value gain on investment property	25	(17,500)	-
Loss on disposal of assets	26	(602)	211
Depreciation on property and equipment	26	109,232	108,717
Write off of property and equipment	26	403	18,358
Right of use depreciation	36	131,253	-
Working capital changes:			
Property inventory		-	(213,729)
Land inventory		38,257	81,449
Other assets		(160,147)	(376,177)
Investment in government securities		555,941	209,944
Loans and advances to customers		1,043,373	289,973
Deposits from banking institutions		(916,926)	470,630
Customer deposits		(2,130,245)	129,398
Related party balances		2,031,869	813,912
Other liabilities		<u>121,816</u>	<u>(22,165)</u>
Cash generated from operations		68,941	838,057
Tax paid	12	<u>(6,970)</u>	<u>(6,313)</u>
Net cash flows generated from operating activities		<u>61,971</u>	<u>831,744</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of intangible assets	24	-	(4,449)
Sale of associate company	22	346,948	-
Purchase of property and equipment	26	<u>(94,110)</u>	<u>(34,028)</u>
Net cash flows from / (used in) investing activities		<u>252,838</u>	<u>(38,477)</u>
CASH FLOWS FROM FINANCING ACTIVITIES			
Repayment of interest-bearing liabilities	30	(815,099)	(416,115)
Repayments of lease liability	36	<u>(133,642)</u>	<u>-</u>
Net cash flows used in financing activities		<u>(948,741)</u>	<u>(416,115)</u>

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
 CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED)
 FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
Net (decrease) / increase in cash and cash equivalents		(633,932)	377,152
Cash and cash equivalents at start of the year		985,323	608,171
Movement in restricted cash balances		<u>-</u>	<u>-</u>
CASH AND CASH EQUIVALENTS AT END OF THE YEAR		<u>351,391</u>	<u>985,323</u>
Cash and cash equivalents comprise: -			
Cash and bank balances	13	168,302	410,440
Placements with financial institutions	14	<u>183,089</u>	<u>574,883</u>

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
 COMPANY STATEMENT OF CASH FLOWS
 FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 KShs'000	2018 KShs'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Loss before taxation		(2,185)	(2,785)
Working capital changes:			
Other assets		475	(519)
Related party balances		946,331	2,001
Other liabilities		<u>(578)</u>	<u>1,232</u>
Cash generated from operations		944,043	(71)
Tax paid	12	<u>-</u>	<u>(32)</u>
Net cash flows from / (used in) operating activities		<u>944,043</u>	<u>(103)</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Additional investment in subsidiary	23	<u>(950,000)</u>	<u>-</u>
Net cash used in financing activities		<u>(950,000)</u>	<u>-</u>
Net decrease in cash & cash equivalents		(5,957)	(103)
Cash and cash equivalents at start of the year		<u>5,974</u>	<u>6,077</u>
CASH AND CASH EQUIVALENTS AT END OF THE YEAR		<u>17</u>	<u>5,974</u>
Cash and cash equivalents comprise: -			
Bank balances	13	17	1,102
Placements with financial institutions	14	<u>-</u>	<u>4,872</u>
		<u>17</u>	<u>5,974</u>

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2019

1. REPORTING ENTITY

Mwalimu National Holdings is incorporated as a limited company in Kenya under the Kenyan Companies Act and is domiciled in Kenya.

The company is a holding company with two subsidiaries as disclosed in note 22, Mwalimu Asset Management Limited (MAM) which is owned 100%, and Equatorial Commercial Holdings Limited which is owned 75%. Equatorial Commercial Holdings Limited (ECH) owns 96% of Spire Bank Limited and 100% of Spire Insurance Brokerage Limited.

The ultimate holding entity is Mwalimu National Savings and Credit Co-operative Society Limited which is incorporated in Kenya under the Co-operative Societies Act Cap 490 and licensed under the Kenyan Sacco Societies Act No 14 of 2008 and is domiciled in Kenya.

2. BASIS OF PREPARATION

(a) Statement of compliance

The consolidated financial statements of the group have been prepared in accordance with International Financial Reporting Standards (IFRS) and the Kenyan Companies Act.

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

The financial statements are prepared on the historical cost basis except for investment properties, which have been measured at fair value.

(b) Use of estimates and judgments

The preparation of financial statements in conformity with International Financial Reporting Standards requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Although these estimates are based on the directors' best knowledge of current events and actions, actual results ultimately may differ from the estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in 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 judgements in applying accounting policies that have the most significant effect on the amounts recognised in financial statements are described in note 6.

(c) Functional and presentation currency

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

3. SIGNIFICANT ACCOUNTING POLICIES

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

(a) Basis of consolidation

(i) Subsidiary

The consolidated financial statements comprise the financial statements of the group and its subsidiaries as at 31 December 2019. The subsidiaries are set out on note 23 while the associates are set out on note 22.

Control is achieved when the group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

Specifically, the group controls a subsidiary if, and only if, the group has:

- Power over the subsidiary (i.e., existing rights that give it the current ability to direct the relevant activities of the investee)
- Exposure, or rights, to variable returns from its involvement with the investee
- The ability to use its power over the investee to affect its returns

Generally, there is a presumption that a majority of voting rights results in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- ▶ The contractual arrangement(s) with the other vote holders of the investee
- ▶ Rights arising from other contractual arrangements
- ▶ The Group's voting rights and potential voting rights

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

Consolidation of a subsidiary begins when the group obtains control over the subsidiary and ceases when the group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed off during the year are included in the consolidated financial statements from the date the group gains control until the date when the group ceases to control the subsidiary.

At company level, the investment in subsidiary is presented as an asset in the statement of financial position and measured at cost.

Profit or loss and each component of OCI are attributed to the owners of the group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the group loses control over a subsidiary, it derecognises the assets (including goodwill), liabilities, non-controlling interest and other components of equity, while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(a) Basis of consolidation (continued)

(ii) Changes in ownership interests in the subsidiary without change of control

Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions - that is, as transactions with the owners in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

(iii) Associates

An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint arrangement. The Group's and company's investment in its associate is accounted for using the equity method of accounting. The associates are set out on note 22.

Under the equity method, the investment in the associate is carried in the statement of financial position at cost plus post-acquisition changes in the Group's and company's share of net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The statement of profit or loss reflects the share of the results of operations of the associate. Where there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes and discloses this, when applicable, in the statement of changes in equity, either directly or through other comprehensive income. Profits or losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

The share of profit of the associate is shown on the face of the statement of profit or loss. This is profit attributable to equity holders of the associate and, therefore, is profit after tax and non-controlling interests in the subsidiaries of the associates after factoring in other comprehensive income.

The financial statements of the associate are prepared for the same reporting period as the Group. Where necessary, adjustments are made to bring its accounting policies in line with the Group. After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on the Group's investment in associates. The Group determines at each reporting date, whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the 'share of profit of an associate' in the statement of profit or loss.

Upon loss of significant influence over the associate, the Group measures and recognises any remaining investment at its fair value. Any differences between the carrying amount of the associate upon loss of significant influence and the fair value of the remaining investment and proceeds from disposal are recognised in profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Revenue recognition

Revenue from contracts with customers

The core principle of IFRS 15 is that an entity will recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

This core principle is delivered in a five-step model framework: [IFRS 15:IN7]

- ◆ Identify the contract(s) with a customer
- ◆ Identify the performance obligations in the contract
- ◆ Determine the transaction price
- ◆ Allocate the transaction price to the performance obligations in the contract
- ◆ Recognise revenue when (or as) the entity satisfies a performance obligation.

Application of this guidance will depend on the facts and circumstances present in a contract with a customer and will require the exercise of judgement.

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the company and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

The specific recognition criteria described below must also be met before revenue is recognised.

Interest income calculates using effective interest rate method

Interest income and expense for all interest bearing instruments are recognised in profit or loss as it accrues, taking into account the effective interest rate of the asset or an applicable floating rate. The effective interest rate is the rate that exactly discounts the estimated future cash flows through the expected life of the financial asset or liability to the carrying amount of the financial asset or liability. Interest income and expense includes the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

When a financial asset becomes credit impaired and is, therefore, regarded as 'Stage 3', the Society calculates interest income by applying the effective interest rate to the net amortised cost of the financial asset. If the financial asset cures and is no longer credit impaired, the society reverts to calculating interest income on gross

(c) Other income

(i) *Fees and commission income*

This mainly relates to fees and commission income including brokerage income is recognized on an accrual basis when the service is provided. This income comprises of appraisal and facility fees charged on advances, commissions charged on use of channels and ledger fees levied on current and savings accounts. The group recognises revenue on fees once they have performed its obligations i.e processed loan, and salaries into the members accounts. The obligation is performed at a point in time and revenue recognised immediately the obligation is performed.

(ii) *Brokerage Income*

Brokerage income, less any discounts payable, is accounted for on the date of inception of the related policy.

(iii) *Foreign exchange trading income*

Foreign exchange trading income comprises gains less losses related to trading assets and liabilities and includes all realized and unrealized exchange gains or losses.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) Other income (continued)

(iv) *Gain or loss on investment property*

Gain or loss on revaluation of investment property is presented as part of net revenue of the Group. The gain is recognised based on the increase or loss in the case of a decrease in market value of the investment property as determined by the Board of Directors through a third party valuation expert at each reporting date. Market value is defined by the International Valuation Standard Committee as the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arms-length transaction after proper marketing wherein the parties have each acted knowledgeably, prudently and without compulsion.

(v) *Sale of land inventory*

Land inventory is regarded as sold when the significant risks and returns have been transferred to the member, which is normally on unconditional exchange of contracts. The fair value of the land inventory property becomes the deemed cost of land inventory. Land inventory is then measured at the lower of cost or net realisable value.

Net realisable value is the estimated selling price in the ordinary course of business, based on market prices at the reporting date and discounted for the time value of money, if material, less costs to completion and the estimated costs of sale.

(vi) *Property inventory*

The Group transfers land from investment property to property inventory when, and only when, there is a change in use evidenced by commencement of development of the relevant precinct with a view to sale. The fair value of the investment property becomes the deemed cost of property inventory. Property inventory is then measured at the lower of cost or net realisable value.

Net realisable value is the estimated selling price in the ordinary course of the business, based on market prices at the reporting date and discounted for the time value of money if material, less costs to completion and the estimated costs of sale.

Cost of related infrastructure is capitalised as part of property inventory and charged against the cost of sales when the related revenue is recognised. The cost of property inventory recognised in profit or loss on disposal is determined with reference to the specific costs incurred on the property sold and an allocation of any non-specific costs based on the relative size of the property sold.

(d) Taxes

Current income tax

Current income tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date.

Current income tax relating to items recognised directly in equity is recognised in equity and not in the statement of profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(d) Taxes (continued)

Deferred tax

Deferred tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date. Deferred tax liabilities are recognised for all taxable temporary differences, except:

- When the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss
- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint arrangements, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future

Deferred tax assets are recognised for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised, except:

- When the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss
- In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint arrangements, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are re-assessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax relating to items recognised outside profit or loss is recognised outside profit or loss. Deferred tax items are recognised in correlation to the underlying transaction either in OCI or directly in equity.

The Group offsets deferred tax assets and deferred tax liabilities if and only if it has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on the same taxable entity.

Value Added Tax

Expenses and assets are recognised net of the amount of value added tax, except:

When the value added tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case, the value added tax is recognised as part of the cost of acquisition of the asset or as part of the expense item, as applicable

- When receivables and payables are stated with the amount of value added tax included.

The net amount of value added tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Fair value measurement

The Group measures financial instruments such as investment properties and unquoted available for sale financial assets at each reporting date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to by the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

External valuers are involved for valuation of significant assets, such as investment properties. Involvement of external valuers is decided upon annually by the finance and investment manager after discussion with and approval by the group's audit committee. Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained.

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Initial recognition and measurement

Financial assets are classified, at initial recognition, as subsequently measured at amortised cost, fair value through other comprehensive income (OCI), and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Group's business model for managing them. The Group initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs.

In order for a financial asset to be classified and measured at amortised cost or fair value through OCI, it needs to give rise to cash flows that are 'solely payments of principal and interest (SPPI)' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

The Group's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the trade date, i.e., the date that the Group commits to purchase or sell the asset.

Subsequent measurement

For purposes of subsequent measurement, financial assets are classified in four categories:

- Financial assets at amortised cost (debt instruments)
- Financial assets at fair value through OCI with recycling of cumulative gains and losses (debt instruments)
- Financial assets designated at fair value through OCI with no recycling of cumulative gains and losses upon derecognition (equity instruments)
- Financial assets at fair value through profit or loss

Financial assets at amortised cost (debt instruments)

This category is the most relevant to the Group. The Group measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

The Group's financial assets at amortised cost include loans to customers and members, cash and cash equivalents, other assets, restricted cash, amounts due from related parties, government securities and placements with financial institutions.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(f) Financial instruments (continued)

Financial assets (continued)

Financial assets at fair value through OCI (debt instruments)

The Group measures debt instruments at fair value through OCI if both of the following conditions are met:

- The financial asset is held within a business model with the objective of both holding to collect contractual cash flows and selling

And

- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding

For debt instruments at fair value through OCI, interest income, foreign exchange revaluation and impairment losses or reversals are recognised in the statement of profit or loss and computed in the same manner as for financial assets measured at amortised cost. The remaining fair value changes are recognised in OCI. Upon derecognition, the cumulative fair value change recognised in OCI is recycled to profit or loss.

The Group's does not have any financial assets classified as debt instruments at fair value through OCI

Financial assets designated at fair value through OCI (equity instruments)

Upon initial recognition, the Group can elect to classify irrevocably its equity investments as equity investments designated at fair value through OCI when they meet the definition of equity under IAS 32 Financial Instruments: Presentation and are not held for trading. The classification is determined on an instrument-by-instrument basis.

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognised as other income in profit or loss when the right of payment has been established, except when the Group benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in OCI. Equity investments designated at fair value through OCI are not subject to impairment assessment.

The Group elected to classify irrevocably its quoted and unquoted equity investments under this category.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading, financial assets designated upon initial recognition at fair value through profit or loss, or financial assets mandatorily required to be measured at fair value. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets with cash flows that are not solely payments of principal and interest are classified and measured at fair value through profit or loss, irrespective of the business model. Notwithstanding the criteria for debt instruments to be classified at amortised cost or at fair value through OCI, as described above, debt instruments may be designated at fair value through profit or loss on initial recognition if doing so eliminates, or significantly reduces, an accounting mismatch.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in the statement of profit or loss.

The Group's does not have any financial assets classified under this category.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial instruments (continued)

Financial assets (continued)

Derecognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Group's statement of financial position) when:

- The rights to receive cash flows from the asset have expired

Or

- The Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Group continues to recognise the transferred asset to the extent of its continuing involvement. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets

The Group recognises an allowance for expected credit losses (ECLs) for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

For trade receivables and contract assets, the Group applies a simplified approach in calculating ECLs. Therefore, the Group does not track changes in credit risk, but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The Group has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Financial assets (continued)

For debt instruments at fair value through OCI, the Group applies the low credit risk simplification. At every reporting date, the Group evaluates whether the debt instrument is considered to have low credit risk using all reasonable and supportable information that is available without undue cost or effort. In making that evaluation, the Group reassesses the internal credit rating of the debt instrument. In addition, the Group considers that there has been a significant increase in credit risk when contractual payments are more than 30 days past due. The Group's debt instruments at fair value through OCI comprise solely of quoted bonds that are graded in the top investment category (Very Good and Good) by the Good Credit Rating Agency and, therefore, are considered to be low credit risk investments. It is the Group's policy to measure ECLs on such instruments on a 12-month basis. However, when there has been a significant increase in credit risk since origination, the allowance will be based on the lifetime ECL. The Group uses the ratings from the Good Credit Rating Agency both to determine whether the debt instrument has significantly increased in credit risk and to estimate ECLs.

The Group considers a financial asset in default when contractual payments are 90 days past due. However, in certain cases, the Group may also consider a financial asset to be in default when internal or external information indicates that the Group is unlikely to receive the outstanding contractual amounts in full before taking into account any credit enhancements held by the Group. A financial asset is written off when there is no reasonable expectation of recovering the contractual cash flows.

Initial recognition and measurement

Financial liabilities

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs. The Group's financial liabilities include members' deposits, withdrawable members' deposits, other payables, borrowings, interest payable and due to related party.

Subsequent measurement

For purposes of subsequent measurement, financial liabilities are classified in two categories:

- Financial liabilities at fair value through profit or loss
- Financial liabilities at amortised cost (loans and borrowings)

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are incurred for the purpose of repurchasing in the near term. This category also includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IFRS 9. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments.

Gains or losses on liabilities held for trading are recognised in profit or loss.

Financial liabilities designated upon initial recognition at fair value through profit or loss are designated at the initial date of recognition, and only if the criteria in IFRS 9 are satisfied. The Group has not designated any financial liability as at fair value through profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Financial assets (continued)

Financial liabilities at amortised cost (loans and borrowings)

This is the category most relevant to the Group. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of profit or loss.

This category generally applies to interest-bearing loans and borrowings and includes customers and members' deposits, other liabilities, and loans and borrowings. For more information, refer to Notes 31, 32 and 33.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in profit or loss.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

(g) Impairment of non-financial assets

The Group assesses, at each reporting date, whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or CGU's fair value less costs of disposal and its value in use. The recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

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. In determining fair value less costs of disposal, recent market transactions are taken into account. If no such transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded companies or other available fair value indicators.

The Group bases its impairment calculation on detailed budgets and forecast calculations, which are prepared separately for each of the Group's CGUs to which the individual assets are allocated. These budgets and forecast calculations generally cover a period of five years. A long-term growth rate is calculated and applied to project future cash flows after the fifth year.

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 DECEMBER 2019

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) Impairment of non-financial assets (continued)

Impairment losses of continuing operations are recognised in profit or loss in expense categories consistent with the function of the impaired asset.

For assets excluding goodwill, an assessment is made at each reporting date to determine whether there is an indication that previously recognised impairment losses no longer exist or have decreased. If such indication exists, the Group estimates the asset's or CGU's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount or exceed the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in profit or loss.

(h) Translation of foreign currencies

The Group's consolidated financial statements are presented in Kenya Shillings (KShs), which is also the parent company's functional currency. For each entity, the Group determines the functional currency and items included in the financial statements of each entity are measured using that functional currency. Transactions in foreign currencies are initially recorded by the Group's entities at their respective functional currency spot rates at the date the transaction first qualifies for recognition.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date. Difference arising on settlement or translation of monetary items are recognised in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. The gain or loss arising on translation of non-monetary items measured at fair value is treated in line with the recognition of the gain or loss on the change in fair value of the item (i.e., translation differences on items whose fair value gain or loss is recognised in OCI or profit or loss are also recognised in OCI or profit or loss, respectively)

(i) Consumables

Consumables are valued at the lower of cost and net realisable value. Cost comprises expenditure incurred in the normal course of business in bringing stocks to their present condition and location. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

(j) Land and property Inventory

Property acquired or being constructed for sale in the ordinary course of business, rather than to be held for rental or capital appreciation, is held as property inventory and is measured at the lower of cost and net realisable value (NRV).

Cost includes:

- Freehold and leasehold rights for land
- Amounts paid to contractors for construction

Non-refundable commissions paid to sales or marketing agents on the sale of real estate units are expensed when paid.

NRV is the estimated selling price in the ordinary course of the business, based on market prices at the reporting date and discounted for the time value of money if material, less estimated costs of completion and the estimated costs necessary to make the sale.

The cost of property inventory recognised in statement of financial position on disposal is determined with reference to the specific costs incurred on the property sold and an allocation of any non-specific costs based on the relative size of the property sold.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(k) Investment property

Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the reporting date. Gains or losses arising from changes in the fair values of investment properties are included in profit or loss in the period in which they arise, including the corresponding tax effect. Fair values are determined based on an annual valuation performed by an accredited external independent valuer.

Investment properties are derecognised either when they have been disposed of or when they are permanently withdrawn from use and no future economic benefit is expected from their disposal. The difference between the net disposal proceeds and the carrying amount of the asset is recognised in profit or loss in the period of derecognition.

Transfers are made to (or from) investment property only when there is a change in use. For a transfer from investment property to owner-occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner-occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

(l) Property and equipment

(i) *Recognition and measurement*

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset.

(ii) *Depreciation*

Depreciation is recognised on a straight-line basis to write down the cost of property and equipment to their residual values over the estimated useful lives of the assets. The rates of depreciation used are based on the following estimated useful lives applicable to the current and prior year:

- Motor vehicles (new)	4 - 7 years
- Motor vehicles (used)	4 - 5 years
- Computer equipment	3 - 4 years
- Office equipment	8 years
- Fixtures and fittings	8 - 12 years
- Office furniture	8 years
- Leasehold improvements	5 - 12 years
- Buildings	40 years or remaining lease period.

Depreciation methods, useful lives and residual values of property and equipment are reviewed at each financial year end and adjusted prospectively, if appropriate.

(iii) *Subsequent costs*

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

(iv) *Derecognition of property and equipment*

An item of property, plant and equipment and any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of profit or loss when the asset is derecognised.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(n) Intangible assets

Intangible assets (computer software and software licences) are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses. The cost incurred to acquire and bring to use specific intangible asset is capitalised, while the costs associated with maintaining the intangible asset is recognised as an expense as incurred.

Intangible assets are amortised on a straight line basis over the expected useful lives, for a period not exceeding five years. The amortisation expense is recognised in the statement of profit or loss in the expense category that is consistent with the function of the intangible assets. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate, and are treated as changes in accounting estimates.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the statement of profit or loss when the asset is derecognised.

(o) 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 asset. All other borrowing costs are expensed in the period in which they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

(p) Leases

The Group has applied IFRS 16 using the modified retrospective approach and therefore the comparative information has not been restated and continues to be reported under IAS 17 and IFRIC 4. The details of accounting policies under IAS 17 and IFRIC 4 are disclosed separately.

The Group recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate.

The Group determines its incremental borrowing rate as the rate of interest the Group would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(p) Leases (continued)

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Group is reasonably certain to exercise, lease payments in an optional renewal period if the Group is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Group is reasonably certain not to terminate early.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured; -

- if there is a change in future lease payments arising from a change in an index or rate,
- if there is a change in the Group's estimate of the amount expected to be payable under a residual value guarantee,
- if the Group changes its assessment of whether it will exercise a purchase, extension or termination option or
- if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The Group presents right-of-use assets in 'property and equipment' and lease liabilities in 'other liabilities' in the statement of financial position.

Short-term leases and leases of low-value assets

The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases. The Group recognises the lease payments associated with these leases as an expense over the lease term.

Policy applicable before 1 January 2019

For contracts entered into before 1 January 2019, the Group determined whether the arrangement was or contained a lease based on the assessment of whether:

- fulfilment of the arrangement was dependent on the use of a specific asset or assets; and
- the arrangement had conveyed a right to use the asset.

Group as a lessee

The Group did not have any finance leases under IAS 17.

Assets held under other leases were classified as operating leases and were not recognized in the Group's statement of financial position. Payments made under operating leases were recognized in profit or loss on a straight-line basis over the term of the lease. Lease incentives received were recognized as an integral part of the total lease expense, over the term of the lease.

Group as a lessor

Leases in which the Group does not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in revenue in the statement of profit or loss due to its operating nature. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(q) Employee benefits

(i) *Defined contribution plan*

The majority of the Group's employees are eligible for retirement benefits under a defined contribution plan. A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and has no legal or constructive obligation to pay further amounts. Contributions to the defined contribution plan are recognised in profit or loss as incurred. Any difference between the amount recognised in profit or loss and the contributions payable is recognised in the statement of financial position under other receivables or other payables. The Group also contributes to a statutory defined contribution pension scheme, the National Social Security Fund (NSSF). Contributions are determined by local statute and are currently limited to KShs 200 per employee per month.

(ii) *Termination benefits*

Termination benefits are recognised as an expense when the Group is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to terminate employment before the normal retirement date. Termination benefits for voluntary redundancies are recognised if the Group has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

(iii) *Short term employee benefits*

Short term employee benefits are expensed as the related service is provided. A liability is recognised for the amount expected to be paid 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.

(r) Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash at banks and on hand and short-term highly liquid deposits with a maturity of three months or less, that are readily convertible to a known amount of cash and subject to an insignificant risk of changes in value.

For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and short-term deposits, as defined above, net of outstanding bank overdrafts as they are considered an integral part of the Group's cash management.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

(s) Sale and repurchase agreement

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, as the Group retains substantially all the risks and rewards of ownership.

The corresponding cash received is recognised in the consolidated statement of financial position as an asset with a corresponding obligation to return it, including accrued interest as a liability within cash collateral on securities lent and repurchase agreements, reflecting the transaction's economic substance as a loan to the Bank.

Securities purchased from the Central Bank of Kenya under agreement to resell (reverse Repos), are disclosed as treasury bonds 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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) New and amended standards and interpretations

The Group applied IFRS 16 Leases for the first time. The nature and effect of the changes as a result of adoption of this new accounting standard is described below.

Several other amendments and interpretations apply for the first time in 2019, but do not have an impact on the consolidated financial statements of the Group. The Group has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective.

IFRS 16-Leases

A. Leases

The Group initially applied IFRS 16 Leases from 1 January 2019. The Group applied IFRS 16 using the modified retrospective approach, under which the cumulative effect of initial application is recognised in retained earnings at 1 January 2019. Accordingly, the comparative information presented for 2018 is not restated - i.e. It is presented, as previously reported, under IAS 17 and related interpretations. The details of the changes in accounting policies are disclosed below. Additionally, the disclosure requirements in IFRS 16 have not generally, been applied to comparative information.

Definition of a lease

Previously, the Group determined at contract inception whether an arrangement was or contained a lease under *IFRIC 4 Determining whether an Arrangement contains a Lease*. The Group now assesses whether a contract is or contains a lease based on the definition of a lease.

On transition to IFRS 16, the Group elected to apply the practical expedient to grandfather the assessment of which transactions are leases. The Group applied IFRS 16 only to contracts that were previously identified as leases. Contracts that were not identified as leases under IAS 17 and IFRIC 4 were not reassessed for whether there is a lease under IFRS 16.

As a lessee

As a lessee, the Group leases assets which include Office spaces. The Group previously classified leases as operating leases under IAS 17 based on its assessment of whether the lease transferred significantly all the risks and rewards incidental to ownership of the underlying asset to the Group. Under IFRS 16, the Group recognises right-of-use assets and lease liabilities for most of these leases - i.e. These leases are on-balance sheet.

At commencement or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component based on its relative stand-alone price. However, the Group has elected not to separate non-lease components and account for the lease and associated non-lease components as a single lease component.

On transition, for these leases, lease liabilities were measured at the present value of the remaining lease payments; discounted at the Group's incremental borrowing rate. Note 5(B)(iv).

MWALIMU NATIONAL HOLDINGS LIMITED AND ITS SUBSIDIARIES
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)
 FOR THE YEAR ENDED 31 DECEMBER 2019

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) New and amended standards and interpretations (continued)

IFRS 16-Leases (continued)

Right-of-use assets are measured at their carrying amount as if IFRS 16 had been applied since the commencement date, discounted using the Group's incremental borrowing rate at the date of initial application. The Group used several practical expedients when applying IFRS 16 to leases previously Classified as operating leases under IAS 17. The Group:

- relied on its assessment of whether leases are onerous under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* Immediately before the date of initial application as an alternative to performing an impairment review.
- did not recognise right-of-use assets and liabilities for leases for which the lease term ends Within 12 months of the date of initial application;
- did not recognise right-of-use assets and liabilities for leases of low value assets.
- excluded initial direct costs from the measurement of the right-of-use asset at the date of initial application
- used hindsight when determining the lease term.

Impact on financial statements

On transition to IFRS 16, the Group recognised additional right-of-use assets, and additional lease liabilities, recognising the difference in retained earnings. The Impact on transition is summarised below.

In thousands of KShs.	01-Jan-19	
	Group	Company
Right-of-use assets	502,159	-
Long Term Lease Liability	368,517	-
Short Term Lease Liability	133,642	-
Retained earnings	-	-

When measuring lease liabilities for leases classified as operating leases, the Group discounted lease payments using its incremental borrowing rate at 1 January 2019.

The incremental borrowing rate used was 13%.

The lease liabilities as at 1 January 2019 can be reconciled to the operating lease commitments as of 31 December 2018 as follows: -

	KShs'000
Operating lease commitments at 31 December 2018	264,193
Weighted average incremental borrowing rate as at 1 Jan 2019	13%
Discounted Operating Lease Commitments as at 1Jan 2019	392,542
Less: Commitments relating to short term leases	-
Commitments relating to LEASES OF Low Value	-
Add: Lease payments relating to renewal period not included in operating lease commitments as at 31 December 2018	<u>109,617</u>
Lease liabilities as at 1 Jan 2019	<u>502,159</u>

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) New and amended standards and interpretations (continued)

IFRIC Interpretation 23 Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 *Income Taxes*. It does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately
- The assumptions an entity makes about the examination of tax treatments by taxation authorities
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates
- How an entity considers changes in facts and circumstances

The Group determines whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments and uses the approach that better predicts the resolution of the uncertainty.

The Group applies significant judgement in identifying uncertainties over income tax treatments. Since the Group operates in a complex multinational environment, it assessed whether the Interpretation had an impact on its consolidated financial statements.

Upon adoption of the Interpretation, the Group considered whether it has any uncertain tax positions, particularly those relating to transfer pricing. The tax filings of the Group and the subsidiaries in different jurisdictions include deductions related to transfer pricing and the taxation authorities may challenge those tax treatments. The Group determined, based on its tax compliance and transfer pricing study, that it is probable that its tax treatments (including those for the subsidiaries) will be accepted by the taxation authorities. The Interpretation did not have an impact on the consolidated financial statements of the Group.

Amendments to IFRS 9: Prepayment Features with Negative Compensation

Under IFRS 9, a debt instrument can be measured at amortised cost or at fair value through other comprehensive income, provided that the contractual cash flows are 'solely payments of principal and interest on the principal amount outstanding' (the SPPI criterion) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI criterion regardless of an event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract. These amendments had no impact on the consolidated financial statements of the Group.

Amendments to IAS 19: Plan Amendment, Curtailment or Settlement

The amendments to IAS 19 address the accounting when a plan amendment, curtailment or settlement occurs during a reporting period. The amendments specify that when a plan amendment, curtailment or settlement occurs during the annual reporting period, an entity is required to determine the current service cost for the remainder of the period after the plan amendment, curtailment or settlement, using the actuarial assumptions used to remeasure the net defined benefit liability (asset) reflecting the benefits offered under the plan and the plan assets after that event. An entity is also required to determine the net interest for the remainder of the period after the plan amendment, curtailment or settlement using the net defined benefit liability (asset) reflecting the benefits offered under the plan and the plan assets after that event, and the discount rate used to remeasure that net defined benefit liability (asset).

The amendments had no impact on the consolidated financial statements of the Group as it did not have any plan amendments, curtailments, or settlements during the period.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) New and amended standards and interpretations (continued)

Amendments to IAS 28: Long-term interests in associates and joint ventures

The amendments clarify that an entity applies IFRS 9 to long-term interests in an associate or joint venture to which the equity method is not applied but that, in substance, form part of the net investment in the associate or joint venture (long-term interests). This clarification is relevant because it implies that the expected credit loss model in IFRS 9 applies to such long-term interests.

The amendments also clarified that, in applying IFRS 9, an entity does not take account of any losses of the associate or joint venture, or any impairment losses on the net investment, recognised as adjustments to the net investment in the associate or joint venture that arise from applying IAS 28 Investments in Associates and Joint Ventures.

These amendments had no impact on the consolidated financial statements as the Group does not have long-term interests in its associate and joint venture

Annual Improvements 2015-2017 Cycle

- IFRS 3 Business Combinations

The amendments clarify that, when an entity obtains control of a business that is a joint operation, it applies the requirements for a business combination achieved in stages, including remeasuring previously held interests in the assets and liabilities of the joint operation at fair value. In doing so, the acquirer remeasures its entire previously held interest in the joint operation.

An entity applies those amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2019, with early application permitted.

These amendments had no impact on the consolidated financial statements of the Group as there is no transaction where joint control is obtained.

Annual Improvements 2015-2017 Cycle (continued)

- IFRS 11 Joint Arrangements

An entity that participates in, but does not have joint control of, a joint operation might obtain joint control of the joint operation in which the activity of the joint operation constitutes a business as defined in IFRS 3.

The amendments clarify that the previously held interests in that joint operation are not remeasured.

An entity applies those amendments to transactions in which it obtains joint control on or after the beginning of the first annual reporting period beginning on or after 1 January 2019, with early application permitted.

These amendments had no impact on the consolidated financial statements of the Group as there is no transaction where a joint control is obtained.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) New and amended standards and interpretations (continued)

- IAS 12 Income Taxes

The amendments clarify that the income tax consequences of dividends are linked more directly to past transactions or events that generated distributable profits than to distributions to owners. Therefore, an entity recognises the income tax consequences of dividends in profit or loss, other comprehensive income or equity according to where it originally recognised those past transactions or events.

An entity applies the amendments for annual reporting periods beginning on or after 1 January 2019, with early application permitted. When the entity first applies those amendments, it applies them to the income tax consequences of dividends recognised on or after the beginning of the earliest comparative period.

Since the Group's current practice is in line with these amendments, they had no impact on the consolidated financial statements of the Group.

- IAS 23 Borrowing Costs

The amendments clarify that an entity treats as part of general borrowings any borrowing originally made to develop a qualifying asset when substantially all of the activities necessary to prepare that asset for its intended use or sale are complete.

The entity applies the amendments to borrowing costs incurred on or after the beginning of the annual reporting period in which the entity first applies those amendments. An entity applies those amendments for annual reporting periods beginning on or after 1 January 2019, with early application permitted.

Since the Group's current practice is in line with these amendments, they had no impact on the consolidated financial statements of the Group.

(u) Standards issued but not yet effective standards issued but not yet effective

The new and amended standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

IFRS 17 Insurance contracts

In May 2017, the IASB issued IFRS 17 *Insurance Contracts* (IFRS 17), a comprehensive new accounting standard for insurance contracts, covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 *Insurance Contracts* (IFRS 4). IFRS 17 applies to all types of insurance contracts (i.e., life, non-life, direct insurance and re-insurance), regardless of the type of entities that issue them, as well as to certain guarantees and financial instruments with discretionary participation features. IFRS 17 is effective for reporting periods beginning on or after 1 January 2021, with comparative figures required. This standard is not applicable to the Group.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(u) Standards issued but not yet effective Standards issued but not yet effective

Amendments to IFRS 3: Definition of a Business

In October 2018, the IASB issued amendments to the definition of a business in IFRS 3 Business Combinations to help entities determine whether an acquired set of activities and assets is a business or not. They clarify the minimum requirements for a business, remove the assessment of whether market participants are capable of replacing any missing elements, add guidance to help entities assess whether an acquired process is substantive, narrow the definitions of a business and of outputs, and introduce an optional fair value concentration test. New illustrative examples were provided along with the amendments. Since the amendments apply prospectively to transactions or other events that occur on or after the date of first application, the Group will not be affected by these amendments on the date of transition.

Amendments to IAS 1 and IAS 8: Definition of Material

In October 2018, the IASB issued amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors to align the definition of 'material' across the standards and to clarify certain aspects of the definition. The new definition states that, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.' The amendments to the definition of material is not expected to have a significant impact on the Group's consolidated financial statements.

4. FINANCIAL RISK MANAGEMENT

The Group's operations are exposed to financial risks. These risks include market risk (including currency risk, fair value, interest rate risk and price risk), credit risk, liquidity risk & cash flow interest rate risk and operational risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

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

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established the Board Audit and Risk Committee and management's Asset and Liability (ALCO) and management Credit and Operational Risk committees, which are responsible for developing and monitoring the Group's risk management policies in their specified areas. 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 Board's Audit and 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 Board's Audit and Risk Committee is assisted in these functions by Internal Audit.

Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Board Audit and Risk Committee.

Although the group is exposed to various risks, the major risks exposures arise due to use of financial instruments and can be categorized as follows:

- (a) Credit risk
- (b) Liquidity risk
- (c) Market risks
- (d) Operational risks.

- (a) Credit risk

Credit risk is the risk that a counterparty will not meet its obligations under a financial instrument or customer contract, leading to a financial loss. The Group is exposed to credit risk from its operating activities (primarily trade receivables) and from its financing activities, including deposits with banks and financial institutions, foreign exchange transactions and other financial instruments.

- i) Mwalimu National Holdings Limited (the company), and Mwalimu Asset Management Limited

The company and Mwalimu Asset Management Limited are exposed to credit risk from its operating activities, that is, from other assets, bank balances and placements with banking institutions.

4. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Credit risk (continued)

i) Mwalimu National Holdings Limited (the company), and Mwalimu Asset Management Limited (continued)

Other assets relates to interest receivable from call deposits and interest receivable due from Spire Bank Limited. An impairment analysis is performed at each reporting date using a provision matrix to measure expected credit losses. The company and Mwalimu Asset Management Limited does not hold collateral as security.

Credit risk from balances with banks and financial institutions is managed by the Group's treasury department in accordance with the Group's policy. Investments of surplus funds are made only with approved counterparties and within credit limits assigned to each counterparty. Counterparty credit limits are reviewed by the Group's Board of Directors on an annual basis and may be updated throughout the year subject to approval of the Group's Finance Committee. The limits are set to minimise the concentration of risks and therefore mitigate financial loss through a counterparty's potential failure to make payments.

ii) Spire Bank Limited

Credit risk is the risk that the Bank will incur a loss because its customers or counterparties fail to discharge their contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

Credit risk is monitored by the credit risk department of the Bank's independent Risk Controlling Unit. It is their responsibility to review and manage credit risk, including environmental and social risk for all types of counterparties. Credit risk consists of line credit risk managers who are responsible for their business lines and manage specific portfolios and experts who support both the line credit risk manager, as well as the business with tools like credit risk systems, policies, models and reporting.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision. The credit quality review process aims to allow the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective actions.

4.1.1. Derivative financial instruments

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded on the statement of financial position. In the case of credit derivatives, the Bank is also exposed to, or protected from, the risk of default of the underlying entity referenced by the derivative. However, to reflect potential losses, the Bank applies portfolio-based debit and credit value adjustments.

With gross-settled derivatives, the Bank is also exposed to a settlement risk, being the risk that the Bank honours its obligation, but the counterparty fails to deliver the counter value.

4.1.2. Credit-related commitments risks

The Bank makes available to its customers guarantees that may require that the Bank makes payments on their behalf and enters into commitments to extend credit lines to secure their liquidity needs. Letters of credit and guarantees (including standby letters of credit) commit the Bank 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 Bank to similar risks to loans and are mitigated by the same control processes and policies.

4. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Credit risk (continued)

ii) Spire Bank Limited (continued)

4.1.3. Impairment assessment

4.1.3.1. Definition of default and cure

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

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

- Internal rating of the borrower indicating default or near-default
- The borrower requesting emergency funding from the Bank
- The borrower having past due liabilities to public creditors or employees
- The borrower is deceased
- A material decrease in the underlying collateral value where the recovery of the loan is expected from the sale of the collateral
- A material decrease in the borrower's turnover or the loss of a major customer
- A covenant breach not waived by the Bank
- The debtor (or any legal entity within the debtor's group) filing for bankruptcy application/protection
- Debtor's listed debt or equity suspended at the primary exchange because of rumours or facts about financial difficulties

It is the Bank's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least six consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition. The Bank's criterion for 'cure' for ECL purposes is less stringent than the 24 months requirement for forbearance

4.1.3.2. The Bank's internal rating and PD estimation process

The Bank's independent Credit Risk Department operates its internal rating models. The Bank runs separate models for its key portfolios in which its customers are rated using the internal rating grades. The models incorporate both qualitative and quantitative information and, in addition to information specific to the borrower, utilise supplemental external information that could affect the borrower's behaviour. These information sources are first used to determine the PDs within the Bank's internal credit rating framework. The internal credit grades are assigned based on performing, watch and non performing grades. PDs are then adjusted for IFRS 9. ECL calculations to incorporate forward looking information and the IFRS 9 Stage classification of the exposure. This is repeated for each economic scenarios as appropriate.

Treasury, trading and interbank relationships

The Bank's treasury, trading and interbank relationships and counterparties comprise financial services institutions, banks, broker-dealers, exchanges and clearing-houses. For these relationships, the Bank's credit risk department analyses publicly available information such as financial information and other external data, e.g., the rating of Rating Agencies, and assigns the internal rating, as shown in the table below

4. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Credit risk (continued)

ii) Spire Bank Limited (continued)

4.1.3.2. The Bank's internal rating and PD estimation process

- Historical financial information together with forecasts and budgets prepared by the client. This financial information includes realised and expected results, solvency ratios, liquidity ratios and any other relevant ratios to measure the client's financial performance. Some of these indicators are captured in covenants with the clients and are, therefore, measured with greater attention.
- Any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies, independent analyst reports, publicly traded bond or CDS prices or press releases and articles.
- Any macro-economic or geopolitical information, e.g., GDP growth relevant for the specific industry and geographical segments where the client operates.
- Any other objectively supportable information on the quality and abilities of the client's management relevant for the company's performance.

The complexity and granularity of the rating techniques varies based on the exposure of the Bank and the complexity and size of the customer. Some of the less complex small business loans are rated within the Bank's models for retail products.

4.1.3.3. Exposure at default

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

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

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

For corporate and investment banking financial instruments, LGD values are assessed at least every three months by account managers and reviewed and approved by the Bank's specialised credit risk department. The credit risk assessment is based on a standardised LGD assessment framework that results in a certain LGD rate. These LGD rates take into account the expected EAD in comparison to the amount expected to be recovered or realised from any collateral held.

The Bank segments its retail lending products into smaller homogeneous portfolios, based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and involves a wider set of transaction characteristics (e.g., product type, wider range of collateral types) as well as borrower characteristics.

Further recent data and forward-looking economic scenarios are used in order to determine the IFRS 9 LGD rate for each group of financial instruments. When assessing forward-looking information, the expectation is based on multiple scenarios. Examples of key inputs involve changes in, collateral values including property prices for mortgages, commodity prices, payment status or other factors that are indicative of losses in the group.

The Bank estimates regulatory and IFRS 9 LGDs on a different basis. Under IFRS 9, LGD rates are estimated for the Stage 1, Stage 2, Stage 3 and POCI IFRS 9 segment of each asset class. The inputs for these LGD rates are estimated and, where possible, calibrated through back testing against recent recoveries. These are repeated for each economic scenario as appropriate.

4. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Credit risk (continued)

ii) Spire Bank Limited (continued)

4.1.3.4 Significant increase in credit risk

The Bank continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Bank assesses whether there has been a significant increase in credit risk since initial recognition. The Bank considers an exposure to have significantly increased in credit risk when the IFRS 9 lifetime PD has doubled since initial recognition and has increased by more than 20 bps a year.

The Bank also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming forborne. In certain cases, the Bank may also consider that events explained in Note 4.1.3.1 are a significant increase in credit risk as opposed to a default. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

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

4.1.4 Analysis of inputs to the ECL model

An overview of the approach to estimating ECLs is set out in Note 3 Summary of significant accounting policies and in Note 6 Significant accounting judgements, estimates and assumptions. To ensure completeness and accuracy, the Bank obtains the data used from a team within Credit Risk Department verifies the accuracy of inputs to the Bank' ECL models including determining the weights attributable to the multiple scenarios. The following tables set out the key drivers of expected loss and the assumptions used for the Bank's base case estimate, ECLs based on the base case, as at 31 December 2018 and 2019.

The tables show the values of the key forward looking economic variables/assumptions used in the ECL calculations. The figures for "Subsequent years" represent a long-term average and so are the same for each scenario.

Assumptions

Key drivers	ECL	Assigned						Subsequent
	Scenario	Probabilities	2020	2021	2022	2023	2024	years
		%	%	%	%	%	%	%
GDP growth %								
	Best (25%)	6.3	4.8	4.8	4.8	4.8	4.8	4.8
	Base case (50%)	6.3	5.7	5.7	5.7	5.7	5.7	5.7
	Worst (25%)	6.3	6.2	6.2	6.2	6.2	6.2	6.2
Inflation								
	Best (25%)	5.6	5.9	5.9	5.9	5.9	5.9	5.9
	Base case (50%)	5.6	6.9	6.9	6.9	6.9	6.9	6.9
	Worst (20%)	5.6	9.7	9.7	9.7	9.7	9.7	9.7

4. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Credit risk (continued)

ii) Spire Bank Limited (continued)

Assumptions (continued)

31 December 2019

*M2 - money supply

1 January 2019

Key drivers	ECL	Assigned						Subsequent
	Scenario	Probabilities	2019	2020	2021	2022	2023	years
		%	%	%	%	%	%	%
M2, % of GDP								
	Best (20%)	32.2	4.0	4.0	4.0	4.0	4.0	4.0
	Base case (60%)	32.2	2.0	2.0	2.0	2.0	2.0	2.0
	Worst (20%)	32.2	-2.0	-2.0	-2.0	-2.0	-2.0	-2.0

4.1.4 Analysis of inputs to the ECL model (continued)

Since the beginning of the year, as the Bank has reassessed the key economic indicators used in its ECL models, the expected M2, % GDP over the next few years has been revised upwards, given the uptick of Kenya's economy. Long-term expectations remain unchanged.

4.1.5 Analysis of risk concentration

The Bank's concentrations of risk are managed by client/counterparty, geographical region and industry sector. The maximum credit exposure to any client or counterparty as of 31 December 2019 was Kshs 293 million (2018: Kshs 264 million), before taking into account collateral, with collateral the bank is not exposed.

4.1.6 Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty.

Guidelines are in place covering the acceptability and valuation of each type of collateral.

The main types of collateral obtained are, as follows:

- For securities lending and reverse repurchase transactions, cash or securities
- For corporate and small business lending, charges over real estate properties, inventory and trade receivables and, in special circumstances, government guarantees

Management monitors the market value of collateral and will request additional collateral in accordance with the underlying agreement.

In its normal course of business, the Bank does not physically repossess properties or other assets in its portfolio, but engages external agents to recover funds, generally at auction, to settle outstanding debt. Any surplus funds are returned to the customers/obligors. As a result of this practice, the residential properties under legal repossession processes are not recorded on the balance sheet and not treated as non-current assets held for sale.

The tables on the following pages show the maximum exposure to credit risk by class of financial asset. They also show the total fair value of collateral, any surplus collateral (the extent to which the fair value of collateral held is greater than the exposure to which it relates), and the net exposure to credit risk.