REPUBLIC OF KENYA

OFFICE OF THE AUDITOR-GENERAL

REPORT

OF

THE AUDITOR-GENERAL

ON

THE FINANCIAL STATEMENTS OF CENTRAL BANK OF KENYA

FOR THE YEAR ENDED 30 JUNE 2017

CENTRAL BANK OF KENYA

ANNUAL REPORT AND
FINANCIAL STATEMENTS

FOR THE YEAR ENDED
30 JUNE 2017

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Board of Directors

Mr. Mohammed Nyaoga	Chairman
Dr. Patrick Njoroge	Governor
Mr. Samson Cherutich	Member
Mrs. Rachel Nzombo	Member
Mrs. Nelius W. Kariuki	Member
Mr. Ravi J. Ruparel	Member
Mrs. Charity S. Kisotu	Member
Dr. Kamau Thugge	Principal Secretary, The National Treasury

Senior Management

Dr. Patrick Njoroge	Governor
Ms. Sheila M'Mbijjewe	Deputy Governor

Heads of Department

Mr. Kennedy Abuga	Director - Governors' Office (Board Secretary)
Ms. Rose Detho	Director - Strategic Management Department
Mr. William Nyagaka	Director - Internal Audit Department
Mr. Charles Koori	Director - Research Department
Mr. Gerald Nyaoma	Director - Bank Supervision Department
Mr. Peter Rotich	Director - Finance and ICT Department-Retired on July 9 ,2017
Mr. Mark Lesiit	Director - Banking, National Payments and Risk Management Department - Retired on November 1, 2016
Mr. John Birech	Acting Director - Financial Markets Department
Ms. Terry Nganga	Acting Director - Human Resource and Administration Department
Mr. Paul Wanyagi	Acting Director - Currency Operations and Branch Administration Department
Mr. Mwenda Marete	Acting Director - Banking, National Payments and Risk Management Department - Appointed on November 9, 2016
Eng. Erastus Miriti	Acting Director - Department of Procurement, Logistics and Supplies - Retired on April 24, 2017
Mr. Peter Kigondu	Acting Director - Department of Procurement, Logistics and Supplies Appointed on April 25,2017
Mr. Moses Ngotho	Acting Director - Finance and ICT Department-Appointed on July 10,2017
Prof. Kinandu Muragu	Executive Director - Kenya School of Monetary Studies-Retired on June 5, 2017
Mr. Joshua Kimoro	Acting Director - Kenya School of Monetary Studies - Appointed on April 19, 2017

Registered office and principal place of business

Central Bank of Kenya Building
Haile Selassie Avenue
P.O. Box 60000
00200 Nairobi, Kenya
Tel.(+254) (020) 2860000

Branches

Mombasa Branch
Central Bank of Kenya Building
Nkurumah Road
P.O. Box 86372
80100 Mombasa

Kisumu Branch
Central Bank of Kenya Building
Jomo Kenyatta Highway
P.O. Box 4
40100 Kisumu

Eldoret Branch
Kiptagich House
Uganda Road
P.O. Box 2710
30100 Eldoret

Currency Centres

Nyeri Currency Centre
Kenya Commercial Bank Building
Kenyatta Street
P.O. Box 840
10100 Nyeri

Meru Currency Centre
Co-operative Bank Building
Njuri Ncheke Street
P.O. Box 2171
60200 Meru

Nakuru Currency Centre
Central Bank of Kenya Building
George Morara Street
P.O. Box 14094
20100 Nakuru

Subsidiary

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1st Ngong Avenue
P.O. Box 51236
00200 Nairobi

Auditor

Deloitte & Touche
Deloitte Place
Waiyaki Way, Muthangari
P.O. Box 40092
00100 Nairobi

On behalf of:-

The Auditor General
Kenya National Audit Office
Anniversary Towers
P.O. Box 30084
00100 Nairobi

1. Statement of Corporate Governance

The Central Bank of Kenya (the "Bank"/"CBK") is wholly owned by the Government of Kenya. The Bank is established by and derives its authority and accountability from Article 231 of the Constitution of Kenya. The Bank is committed to maintaining the highest standards of integrity, professionalism and business ethics in all its operations.

1.1 Board of Directors

The Central Bank of Kenya Act (the "Act") provides that the Board of Directors (the "Board") shall be composed of a Chairperson, a Governor, Principal Secretary to The National Treasury who is a non-voting member and eight Non-Executive Directors. The law requires that the President appoints the Chairman and Governor after the conduct of a competitive process and following the approval of Parliament. Other than the Principal Secretary to The National Treasury who is an ex-officio member, all the Non-Executive Directors of the Board are also appointed by the President with the approval of Parliament. All the Board members are appointed for a term of four (4) years each and are eligible for reappointment provided that no Board member holds office for more than two (2) terms.

All the Non-Executive Directors are independent of management and free from any business or other relationship, which could interfere with the exercise of their independent judgement.

The Board meets once every two (2) months and has a formal schedule of agenda items due for deliberations. The Directors are given appropriate and timely information to enable them provide and maintain full and effective direction and control over strategic, financial and operational issues of the Bank. The Board is not involved in the conduct of day-to-day business as this is the responsibility given to the Governor by law. It however, retains responsibility for determining the policies of the Bank.

The Members of the Board (all Kenyans) in the year ended 30th June, 2017 and their attendance and the number of meetings held in the year were as follows:

No.	Name	Position	Discipline	Date of Appointment / Retirement	Meetings Attended
1.	Mr. Mohammed Nyaoga	Chairman	Lawyer	Appointed – 19th June, 2015	4
2.	Dr. Patrick Njoroge	Governor	Economist	Appointed – 19th June 2015	4
3.	Principal Secretary/ National Treasury	Executive Officer	Economist	Permanent	2
4.	Mrs. Nelius Kariuki	Member	Economist	Appointed – 4th November, 2016	4
5.	Mr. Ravi Ruparel	Member	Financial Sector Expert	Appointed – 4th November, 2016	3
6.	Mrs. Charity Kisotu	Member	Accountant	Appointed – 4th November, 2016	4
7.	Mr. Samson Cherutich	Member	Accountant	Appointed – 5th December, 2016	4
8.	Mrs. Rachel Dzombo	Member	Management Expert	Appointed – 5th December, 2016	4

The remuneration paid to the Directors for services rendered during the financial year 2016/2017 is disclosed in Note 28 to the financial statements. The Non-Executive Directors are paid a monthly retainer fee and a sitting allowance for every meeting attended. There were no loans to Non-Executive Directors during the year while Executive Directors are paid a monthly salary and are eligible for staff loans.

1.2 Secretary to the Board

The Board Secretary provides technical and secretarial services as well as corporate governance and logistical support to the Board in order to facilitate efficient policy making interface with policy implementation. The Board Secretary also advises the Board on legal matters. In conjunction with the Chairman, the Board Secretary ensures good and timely information flow among the Board members, the Board Committees and Management. All members of the Board and Management have access to the Board Secretariat services.

1.3 Audit Committee

The members of the Audit Committee in the year ended 30th June, 2017 were Mr. Samson K. Cherutich (Chairman), Mr. Ravi J. Ruparel, Mrs. Charity S. Kisotu and Mrs. Nelius W. Kariuki. They were appointed to the Committee by the Board of Directors on 6th April, 2017. The members are all Non-Executive Directors with experience in Accounting, Auditing, Financial and Business Management. The Committee meets once every two (2) months and as necessary. The Terms of Reference of the Audit Committee cover five (5) major areas, namely; Internal Control System, Financial Reporting and Related Reporting Practices, External and Internal Audits.

The Audit Committee's mandate, under Internal Control, includes ensuring that the importance of internal control and risk management is communicated effectively to staff and that they have a clear understanding of their roles and responsibilities. It will also ensure that the Management has put in place adequate measures to ensure security of the bank's information technology resources and that appropriate contingency plans for processing the Bank's information in the event of unavailability of the IT resources are in existence. The Committee also ensures that internal and external audit recommendations are implemented.

The mandate relating to Financial Reporting and Related Reporting Practices requires the Audit Committee to review the annual financial statements of the Bank, the external auditor's opinion and their comments on internal controls and other observations. The Committee also reviews significant accounting and reporting issues and their impact on financial reports and legal matters that could significantly impact on the financial statements, among other financial reporting responsibilities.
With regard to External Audit, the Audit Committee reviews the external auditor's proposed audit scope, approach and audit deliverables, and reviews the financial statements before submission to the Board for consideration and approval.

The Committee's mandate on Internal Audit covers review of the activities and resources of the internal audit activity, including the effectiveness, standing and independence of the internal audit function within the Bank. It also covers review of the internal audit plan and follow up of the implementation of internal auditor findings and recommendations. The Audit Committee reports to the Board of Directors on the standing and independence of the internal audit function within the Bank. The Audit Committee also reports to the Board of Directors on internal audit scope, approach and deliverables.

The Committee Members' positions, disciplines and number of meetings attended for the year ended 30th June 2017 were as follows:

No.	Name	Position	Discipline	Meetings Attended
1.	Mr. Samson Cherutich	Chairman of the Committee with effect from April 6, 2017	Accountant	2
2.	Mr. Ravi Ruparel	Member effective from April 6, 2017	Financial Sector Expert	2
3.	Mrs. Charity Kisotu	Member effective from April 6, 2017	Accountant	2
4.	Mrs. Nelius Kariuki	Member effective from April 6, 2017	Economist	2

1.4 Human Resources Committee (HRC)

The members of the HR Committee in the year ended 30th June, 2017 were Mrs Nelius Kariuki, Mr Samson Cherutich, Mrs Charity Kisotu and Mrs Rachel Dzombo. The members are all Non-Executive Directors with experience in Accounting, Management and Business.

The mandate of the HR Committee is to perform an advisory role to the Board in the fulfilment of the following oversight role:

a) Overseeing the formulation and implementation of the HR Policies of the Bank;
b) Overseeing the Bank's compliance with the Constitution of Kenya 2010, Laws of Kenya, CBK regulations and the Code of Conduct;
c) Performing any other HR related function assigned by the Board;
d) Overseeing the implementation of the Board resolutions relating to the HR Committee.

The members of the Human Resources Committee in the year ended 30th June, 2017 and their attendance of the meetings held in the year were as follows:

No.	Name	Position	Discipline	Meetings Attended
1	Mrs. Nelius Kariuki	Chairperson	Economist	1
2	Mr. Samson Cherutich	Member	Accountant	1
3	Mrs. Charity Kisotu	Member	Accountant	1
4	Mrs Rachel Dzombo	Member	Management Expert	1

The HR Committee was constituted on April 2017 and held its first meeting on 24th May 2017.

1.5 Monetary Policy Committee (MPC)

Section 4D of the Central Bank of Kenya (Amendment) Act 2008 establishes the Monetary Policy Committee (MPC). The MPC is responsible for formulating monetary policy and is required to meet at least once in two (2) months. External members of the MPC are appointed by the Cabinet Secretary to The National Treasury for an initial period of three (3) years each, and may be reappointed for another final term of three (3) years.

During the FY2016/17, the MPC formulated monetary policy to achieve and maintain overall inflation within the allowable margin of 2.5 percent on either side of the 5 percent target. The period was characterised by amongst other factors, uncertainties with regard to the impact of interest rate capping on the economy and on the effectiveness of monetary policy; a persistent slowdown in the growth of private sector credit and a sharp increase in food prices due to drought conditions experienced in the first quarter of 2017. Overall month-on-month inflation remained within the Government target range from July 2016 to January 2017, but rose above the target range in February 2017, peaking at 11.7 percent in May 2017. The Government instituted measures to mitigate the adverse effects of the drought on key food items, including zero-rating of taxes on maize and bread, duty free imports of maize and sugar. The impact of the Government interventions to lower prices of key food items and price responses to improved weather conditions were reflected in a fall in overall inflation to 9.2 percent in June 2017. The 12-month and 3-month non-food-non-fuel inflation measures remained stable, suggesting that there were no demand pressures in the economy.

Risks in the global financial markets remained elevated in the period due to uncertainties on the direction of United States of America (USA) economic and trade policies, normalization of monetary policies in the advanced economies and the British Exit from the European Union (Brexit) outcome. Kenya's foreign exchange market remained stable in the period reflecting a narrowing in the current account deficit due to resilient inflows from tea and horticultural exports, strong diaspora remittances, improved receipts from tourism and a lower import bill. CBK's foreign exchange reserves, together with the Precautionary Arrangements with the IMF provided a buffer against short-term shocks.

1.5 Monetary Policy Committee (MPC) (Continued)

After every MPC Meeting, the Governor held meetings with Chief Executive Officers of banks to discuss the background to the MPC decisions and to obtain feedback from the market. Additionally, the Governor held press conferences with the media to brief them on the background of the MPC decisions and developments in the financial sector. The forums continued to improve the public's understanding of monetary policy decisions.

The MPC held six (6) meetings in the year ended June 30, 2017, and attendance was as follows:

No.	Name	Position	Discipline	Meetings Attended
1	Dr. Patrick Njoroge	Chairman	Economist	6
2	Ms. Sheila M'Mbijjewe	Vice Chairperson	Finance/ Accountancy	6
3	Mr. Nzomo Mutuku *	Representative of the Principal Secretary, The National Treasury	Economist	3
4	Mr. Musa Kathanje *	Representative of the Principal Secretary, The National Treasury	Economist	1
5	Prof. Francis Mwega **	Member	Economist	3
6	Mrs. Farida Abdul ***	Member	Economist	5
7	Mr. Charles Koori	Member (Internal)	Economist	6
8	Mr. John Birech	Member (Internal)	Economist	6

** Mr. Kathanje replaced Mr. Nzomo as the Representative of the Principal Secretary of The National Treasury in May 2017.*
*** Prof. Mwega's term ended on February 28, 2017.*
**** Mrs. Abdul's term ended on April 30, 2017.*

1.6 Management Structure

The positions of Governor and Deputy Governor are set out in the CBK Act Cap 491 of the Laws of Kenya. The Governor and the Deputy Governor constitute the Central Bank's Senior Management and meet regularly with the Heads of the Bank's various departments indicated on page 1, to review the overall performance of the Bank.

There are several other Management Committees, which advise the Governor on specific issues to enable him discharge his responsibilities as the Chief Executive Officer of the Bank.

1.7 Code of Ethics

The Bank is committed to the highest standards of integrity, behaviour and ethics. A formal code of ethics for all employees has been approved by the Board and is fully implemented. All employees of the Bank are expected to avoid activities and financial interests, which could give rise to conflict of interest with their responsibilities in the Bank. Strict rules of conduct embedded in the *Staff Rules and Regulations* and *the Employment Act 2007* apply to the entire Bank's staff.

1.8 Internal Controls

The Management of the Bank has put in place a systems of internal control mechanisms to ensure the reporting of complete and accurate accounting information. Procurement of goods and services is strictly done in accordance with the *Public Procurement & Disposal Act, 2015*. In all operational areas of the Bank, workflows have been structured in a manner that allows adequate segregation of duties.

1.9 Authorizations

All the expenditure of the Bank must be authorized in accordance with a comprehensive set of the Bank policies and procedures. There is an annual Budget approved by the Board and a Procurement Plan approved by the Senior Management before commencement of the financial year. The Board of Directors receives regular management accounts comparing actual outcomes against budget as a means of monitoring actual financial performance of the Bank.

1.10 Internal Audit and Risk Management

The internal audit function is performed by Internal Audit Department. The Risk Management Unit is a separate function under Banking Department and is responsible for monitoring and providing advice on the Bank’s risk management framework. All reports of Internal Audit Department and Risk Management Unit are availed to the Audit Committee of the Board.

1.11 Transparency

The Bank publishes an Annual Report, Monthly Economic Review, Weekly Releases, Statistical Bulletin and Bi-annual Monetary Policy Statement which explain current monetary policy and also, provide the expected monetary policy stance. In addition, the Bank issues policy briefs to The National Treasury on both the Monetary and Fiscal policies. On an annual basis, the Financial Statements of the Bank are published in the Kenya Gazette and are also placed in the Bank’s website.

2. Financial Performance

The Bank's financial performance is affected by Monetary Policy undertaken, interest rates and exchange rate changes. The Bank's financial performance is presented on page 14 of these financial statements.

During financial year ended 30 June, 2017, the Bank recorded a net surplus of Shs.17,050 million compared to a net deficit of Shs.4,640 million in financial year ended 30 June, 2016. The surplus has been added to the General Reserve Fund.

During the financial year ended 30 June, 2017, the Bank's net interest income after impairment charge was Shs.12,747 million (2016: Shs.11,917 million) subject to the Loan impairment adjustment. Interest income was Shs.14,441 million (2016: Shs.15,933 million). Interest earnings on foreign reserves was Shs.7,070 million (2016: Shs.4,065 million). The increase is attributed to relatively higher interest rates on term deposits, foreign reserve build up partly from loan receipts by the Government and optimization of reserve currency mix. Interest earned on loans and advances was Shs.7,011 million(2016: Shs.10,858 million). The drop is due to reduced utilization of Government of Kenya overdraft facility and also, reduced advances to commercial banks due to a relatively more stable market during the year as compared to the previous year.

The interest expense was Shs.1,718 million (2016: Shs.3,957 million). The main contributor is the drop in Interest on monetary policy to Shs.1,445 million (2016: Shs.3,819 million) attributed to the monetary policy stance of relatively stable markets compared to previous year. The unrealized foreign exchange gain was Shs.8,516 million (2016 Loss Shs.19,969 million). This resulted from movement of the Kenya shilling to the USD between the two periods. In the previous year, the shilling had strengthened against the British Pound and hence the loss recorded.

2. Financial Performance (continued)

Trading income generated from sale of foreign currency is Shs.4,298 million (2016: Shs.6,496 million). The market was relatively stable compared to the previous year resulting in low volumes of sale of foreign currency during the period.

Operating expenses increased to Shs.11,137 million (2016: Shs.8,091 million) as a result of revaluation gains arising from retirement benefits assets of Shs.832 million (2016: Shs.1,835 million). In addition, Currency costs increased during the year to Shs.2,352 million (2016:Shs. 1,880 million) due to higher releases of currency notes and coins.

The Bank's Consolidated Statement of financial position for the year is set out on page 15.

The Bank's assets decreased marginally to Shs.975,623 million (2016: Shs.982,849 million) which is attributed mainly to the more than offset of, the increase in balances due from banking institutions Shs.735,548 million (2016: Shs.696,004 million), by decrease in both Securities & advances to banks Shs.34,870 (2016: Shs.44,675) and Government overdraft Shs.24,449 million (2016: Shs.69,762 million).

Liabilities also decreased to Shs.841,580 million (2016: 865,856 million) attributed to the decrease in deposits from banks and the Government which was largely contributed by the full repayment of government overdraft facility and the decline of Reverse Repo (Repurchase Agreements) investment by commercial banks.

Director's Report

The Directors submit their report together with the audited Financial Statements for the year ended 30th June 2017, which shows the state of affairs of Central Bank of Kenya (the "Bank"/"CBK").

Incorporation

The Bank is incorporated under Article 231 of the Constitution of Kenya, 2010.

Principal Activities

The Bank is established and administered under the Constitution of Kenya, 2010 with the principal object of formulating and implementing monetary policy directed to achieving and maintaining stability in the general level of prices. It is also the responsibility of the Bank to foster liquidity, solvency and proper functioning of a stable market-based financial system. The Bank also acts as banker, advisor and fiscal agent of the Government of Kenya.

Results and Surplus

The surplus for the year of Shs.17,050 million (2016: Shs.4,640 million deficit) has been added to the General Reserve Fund. The Directors do not recommend distribution of surplus (2016: Nil).

Board of Directors

The members of the Board of Directors who served during the year and up to the date of this report are listed on page 1.

Auditor

The Bank is audited by the Auditor General in accordance with *Section 12 of the Public Audit Act* and the *Central Bank of Kenya Act*.

By order of the Board

Kennedy Abuga
Board Secretary

6th September 2017

The Directors are responsible for the preparation of Financial Statements for each financial year that give a true and fair view of the state of affairs of the Bank as at the end of the financial year and of the Bank's surplus or deficit. The Directors also ensure that the Bank keeps proper accounting records that disclose, with reasonable accuracy, the financial position of the Bank. They are also responsible for safeguarding the assets of the Bank.

The Directors accept responsibility for the preparation and fair presentation of Financial Statements that are free from material misstatements whether due to fraud or error. They also accept responsibility for:

(i) Designing, implementing and maintaining internal control necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error;

(ii) Selecting and applying appropriate accounting policies; and

(iii) Making accounting estimates and judgments that are reasonable in the circumstances.

The Directors are of the opinion that the financial statements give a true and fair view of the state of the financial position of the Bank as at 30th June 2017 and of the Bank's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the *Central Bank of Kenya Act*.

Nothing has come to the attention of the Directors to indicate that the Bank and its subsidiary will not remain a going concern for at least twelve (12) months from the date of this statement.

Approved by the Board of Directors and signed on its behalf by:

Chairman, Board of Directors
Mr. Mohammed Nyaoga

8th September 2017

Patrick Njoroge

Governor
Dr. Patrick Njoroge

8th September 2017

REPUBLIC OF KENYA

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OFFICE OF THE AUDITOR-GENERAL

REPORT OF THE AUDITOR-GENERAL ON CENTRAL BANK OF KENYA FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

OPINION

The accompanying financial statements of Central Bank of Kenya set out on pages 14 to 57, which comprise the consolidated statement of financial position as at 30 June 2017, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information have been audited on my behalf by Delloitte and Touche, auditors appointed under Section 23 of the Public Audit Act, 2015 and in accordance with the provisions of Article 229 of the Constitution of Kenya. The auditors have duly reported to me the results of their audit and on the basis of their report, I am satisfied that all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit were obtained.

In my opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Central Bank of Kenya as at 30 June 2017, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) and comply with the Central Bank Act, Cap 491 of the Laws of Kenya.

Basis for Opinion

The audit was conducted in accordance with International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the Auditor-General's Responsibilities for the audit of financial statements section of my report. I am independent of the Bank in accordance with the International Ethics Standard Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), together with other ethical requirements that are relevant to the audit of financial statements in Kenya. I have fulfilled my other ethical responsibilities in accordance with these requirements, and IESB Code. I believe that the audit evidence obtained is sufficient and appropriate to provide a basis for my opinion.

Other Information

The Directors are responsible for the other information, which comprises the statement of corporate governance, directors' report and the statement of Directors' responsibilities. The other information does not include the financial statements and my auditor's report thereon.

My opinion on the consolidated financial statements does not cover the other information and I do not express any form of assurance or conclusion thereon.

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

Responsibilities of the Directors and Those Charged With Governance for the Financial Statements

The Directors are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with IFRSs, and for such internal control as Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Directors are responsible for assessing the Bank'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 Bank or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

The audit objectives are to obtain reasonable assurance about whether the consolidated 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 my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229 of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect material misstatements when they exist. 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 financial statements.

As part of audit in accordance with ISAs, the auditor exercises professional judgement and maintains professional scepticism throughout the audit. The auditor also:

- Identifies and assesses the risk of material misstatement of the consolidated financial statements, whether due to fraud or error, designs and performs audit procedures responsive to those risks, and obtains audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting material misstatements resulting from fraud is higher than one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentation, or the override of internal control;
- obtains an understanding of the 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 Bank's internal control;
- evaluates the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors;
- concludes on the appropriateness of the Directors use of going concern basis of accounting and, based on the audit evidence obtained, concludes whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If the auditor concludes that a material uncertainty exists, the auditor is required to draw attention in the auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify the opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern;
- evaluates the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- obtains sufficient appropriate audit evidence regarding the consolidated financial information of the entity or business activities within the Bank to express an opinion on the consolidated financial statements. The auditor is responsible for the direction, supervision and performance of the audit. I remain responsible for the audit opinion;
- communicates with directors among other matters, the planned scope and timing of the audit and significant audit findings, including any significant audit deficiencies in internal control that are identified during the audit.

FCPA Edward R. O. Ouko, CBS
<u>AUDITOR-GENERAL</u>

Nairobi

22 September 2017

Consolidated Statement of Comprehensive Income

	Notes	Year ended 30 June 2017 Shs' million	2016 Shs' million
Interest income	4	14,441	15,933
Interest expense	5	(1,718)	(3,957)
Net interest income		12,723	11,976
Decrease/(increase) in loan impairment	15	24	(59)
Net interest income		12,747	11,917
Fees and commission income	2(s)	3,000	3,000
Net trading income	6	4,193	6,446
Other income	7	1,114	536
Operating income		21,054	21,899
Operating expenses	8	(11,137)	(8,091)
Operating surplus before unrealised gains/(losses)		9,917	13,808
Items that will not be reclassified subsequently to profit or loss:			
Unrealized gains and losses:			
Foreign exchange gain/(loss)		8,516	(19,969)
Fair value (loss)/gain on financial assets held for trading		(871)	347
Surplus/(deficit) for the year		17,562	(5,814)
Other comprehensive income			
Actuarial (loss)/gain in retirement benefit asset	17	(512)	1,174
Total comprehensive income/(loss) for the year		17,050	(4,640)

The notes on pages 19 to 57 are an integral part of these financial statements.

Consolidated Statement of Financial Position

	Notes	30 June 2017 Shs' million	30 June 2016 Shs' million
Assets			
Balances due from banking institutions	10	735,548	696,004
Funds held with International Monetary Fund (IMF)	13(a)	1,877	1,923
Securities & advances to banks	14	34,870	44,679
Loans and advances	15	2,575	2,566
Financial assets at fair value through profit or loss	11	134,777	133,253
Investments securities – Available-for-sale	12	9	9
Other assets	16	10,566	4,285
Property and equipment	18	22,703	22,385
Intangible assets	19	52	207
Retirement benefit asset	17	8,197	7,776
Due from Government of Kenya	20	24,449	69,762
Total assets		975,623	982,849
Liabilities			
Currency in circulation	21	253,787	234,751
Deposits from banks and government	22	470,109	496,044
Due to International Monetary Fund (IMF)	13(b)	115,125	122,438
Investments by banks	23	-	7,843
Other liabilities	24	2,559	4,780
Total liabilities		841,580	865,856
Equity and reserves			
Share capital	25(a)	5,000	5,000
General reserve fund	25(b)	114,253	97,203
Revaluation reserve	25(c)	14,790	14,790
Total equity		134,043	116,993
Total equity and liabilities		975,623	982,849

The financial statements on pages 14 to 57 were authorised for issue by the Board of Directors on 8th September 2017 and signed on its behalf by:

Chairman of the Board
Mr. Mohammed Nyaoga

Patrick Njoroge
Governor
Dr. Patrick Njoroge

Consolidated Statement of Changes in Equity

	Notes	Share Capital Shs' million	General Reserve Fund Shs' million	Revaluation reserve Shs' million	Total Shs' million
Year ended 30 June 2016					
Balance at 1 July 2015		5,000	101,843	14,790	121,633
Deficit for the year		-	(5,814)	-	(5,814)
Actuarial gains in retirement benefit asset	17	-	1,174	-	1,174
Total comprehensive loss for the year		-	(4,640)	-	(4,640)
Balance at 30 June 2016		**5,000**	**97,203**	**14,790**	**116,993**

The notes on pages 19 to 57 are an integral part of these financial statements.

Consolidated Statement of Changes in Equity (continued)

	Notes	Share Capital Shs' million	General Reserve Fund Shs' million	Revaluation reserve Shs' million	Total Shs' million
Year ended 30 June 2017					
Balance at 1 July 2016		5,000	97,203	14,790	116,993
Surplus for the year		-	17,562	-	17,562
Actuarial loss on retirement benefit asset		-	(512)	-	(512)
Total comprehensive income for the year		-	17,050	-	17,050
Balance at 30 June 2017		**5,000**	**114,253**	**14,790**	**134,043**

The notes on pages 19 to 57 are an integral part of these financial statements.

Consolidated Statement of Cash Flow

	Notes	Year ended 30 June 2017 Shs' million	2016 Shs' million
Net cash generated from operating activities	26	39,820	172,352
Cash flow from investing activities			
Purchase of property and equipment	18	(1,273)	(2,592)
Purchase of intangible assets	19	(24)	-
Proceeds from disposal of property and equipment		3	8
Net (purchase)/sale of financial assets			
- Fair value through profit or loss		(10,464)	(9,309)
- Held to maturity	10	150,515	69,906
- Securities & advances to the Bank		(8,508)	(2,762)
- Funds held with International Monetary Fund (IMF)		46	2,462
Net cash generated from investing activities		130,295	57,713
Cash flows from financing activities			
Repayments to the International Monetary Fund (IMF)		(7,313)	(3,337)
Net cash used in financing activities		(7,313)	(3,337)
Increase in cash and cash equivalents		162,802	226,728
Cash and cash equivalents at start of year		421,593	194,865
Cash and cash equivalents at end of year	27	584,395	421,593

The notes on pages 19 to 57 are an integral part of these financial statements.

Notes to the Financial Statements (continued)

1 General information

Central Bank of Kenya (the "Bank"/"CBK") is established by and derives its authority and accountability from the *Central Bank of Kenya Act*, *Cap 491* of the Laws of Kenya (the "CBK Act"). The Bank is wholly owned by the Government of Kenya and is domiciled in Kenya. The Bank acts as banker, advisor and agent of the Government of Kenya.

2 Summary of significant accounting policies

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

(a) Basis of preparation

The financial statements are prepared in compliance with International Financial Reporting Standards (IFRS). The measurement basis applied is the historical cost basis, except where otherwise stated in the accounting policies below. The financial statements are presented in Kenya Shillings (KShs), rounded to the nearest million.

Changes in accounting policy and disclosures

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC)

i) *New standards and amendments to published standards effective for the year ended 30 June 2017*

IFRS 14: Regulatory Deferral Accounts

IFRS 14 permits an entity which is a first-time adopter of International Financial Reporting Standards to continue to account, with some limited changes, for 'regulatory deferral account balances' in accordance with its previous GAAP, both on initial adoption of IFRS and in subsequent financial statements.

Applicable to annual periods beginning on or after 1 January 2016. The application of this Standard has had no effect on the consolidated financial statements.

Amendments to IFRS 11

Amends IFRS 11 Joint Arrangements to require an acquirer of an interest in a joint operation in which the activity constitutes a business (as defined in IFRS 3 Business Combinations) to:

- apply all of the business combinations accounting principles in IFRS 3 and other IFRSs, except for those principles that conflict with the guidance in IFRS 11; and
- disclose the information required by IFRS 3 and other IFRSs for business combinations

Applicable to annual periods beginning on or after 1 January 2016. The application of these amendments has had no effect on the consolidated financial statements.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC) (Continued)

i) *New standards and amendments to published standards effective for the year ended 30 June 2017 (Continued)*

Amendments to IAS 16: Property, Plant and Equipment and IAS 38: Intangible Assets

Amends IAS 16 and IAS 38 to:

- clarify that a depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is not appropriate for property, plant and equipment;
- introduce a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate, which can only be overcome in limited circumstances where the intangible asset is expressed as a measure of revenue, or when it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated; and
- add guidance that expected future reductions in the selling price of an item that was produced using an asset could indicate the expectation of technological or commercial obsolescence of the asset, which, in turn, might reflect a reduction of the future economic benefits embodied in the asset.

Applicable to annual periods beginning on or after 1 January 2016. The application of these amendments has had no effect on the consolidated financial statements.

Amendments to IAS 16: Property, Plant and Equipment and IAS 41: Agriculture

Amends IAS 16 Property, Plant and Equipment and IAS 41 Agriculture to:

- include 'bearer plants' within the scope of IAS 16 rather than IAS 41, allowing such assets to be accounted for a property, plant and equipment and measured after initial recognition on a cost or revaluation basis in accordance with IAS 16;
- introduce a definition of 'bearer plants' as a living plant that is used in the production or supply of agricultural produce, is expected to bear produce for more than one period and has a remote likelihood of being sold as agricultural produce, except for incidental scrap sales; and
- clarify that produce growing on bearer plants remains within the scope of IAS 41.

Applicable to annual periods beginning on or after 1 January 2016. The application of these amendments has had no effect on the consolidated financial statements.

Amendments to IAS 27: Separate Financial Statements

Amends IAS 27 to permit investments in subsidiaries, joint ventures and associates to be optionally accounted for using the equity method in separate financial statements.

Applicable to annual periods beginning on or after 1 January 2016. The application of these amendments has had no effect on the consolidated financial statements.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC) (Continued)

ii) *New standards and amendments to published standards effective for the year ended 30 June 2017 (Continued)*

Amendments to IFRS 10: Consolidated Financial Statements and IAS 28: Investments in Associates and Joint Ventures (2011)

Amends IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures (2011) to clarify the treatment of the sale or contribution of assets from an investor to its associate or joint venture, as follows:

- require full recognition in the investor's financial statements of gains and losses arising on the sale or contribution of assets that constitute a business (as defined in IFRS 3 Business Combinations); and
- require the partial recognition of gains and losses where the assets do not constitute a business, i.e. a gain or loss is recognised only to the extent of the unrelated investors' interests in that associate or joint venture.

Applicable to annual periods beginning on or after 1 January 2016. The application of these amendments has had no effect on the consolidated financial statements.

Annual Improvements to IFRSs 2012-2014 Cycle

The Annual Improvements to IFRSs 2012-2014 Cycle include a number of amendments to various IFRSs, which are summarised below:

IFRS 5, Non-current Assets Held for Sale and Discontinued Operations- The amendments introduce specific guidance in IFRS 5 for when an entity reclassifies an asset or disposal group) from held for sale to held for distribution to owners (or vice versa). The amendments clarify that such a change should be considered as a continuation of the original plan of disposal and hence requirements set out in IFRS 5 regarding the change of sale plan do not apply. The amendments also clarifies the guidance for when held-for- distribution accounting is discontinued.

IFRS 7, Financial Instruments: Disclosures - The amendments provide additional guidance to clarify whether a servicing contract is continuing involvement in a transferred asset for the purpose of the disclosures required in relation to transferred assets.

IAS 19, Employee Benefits (2011) - The amendments clarify that the rate used to discount post-employment benefit obligations should be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. The assessment of the depth of a market for high quality corporate bonds should be at the currency level (i.e. the same currency as the benefits are to be paid). For currencies for which there is no deep market in such high quality corporate bonds, the market yields at the end of the reporting period on government bonds denominated in that currency should be used instead.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC) (Continued)

ii) New and amended standards in issue but not yet effective in the year ended 30 June 2017

New standards and Amendments to standards	*Effective for annual periods beginning on or after*
IFRS 9 Financial Instruments	1 January 2018
IFRS 15 Revenue from contracts with customers	1 January 2018
IFRS 16 Leases	1 January 2019
Amendments to IAS 7 Statement of Cash Flows	1 January 2017

IFRS 9: Financial Instruments

IFRS 9, issued in November 2009, introduced new requirements for the classification and measurement of financial assets. IFRS 9 was amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for de-recognition.

Key requirements of IFRS 9:

Classification and measurement

Financial assets are classified by reference to the business model within which they are held and their contractual cash flow characteristics. The 2014 version of IFRS 9 introduces a 'fair value through other comprehensive income' category for certain debt instruments. Financial liabilities are classified in a similar manner to under IAS 39, however there are differences in the requirements applying to the measurement of an entity's own credit risk.

Impairment

The 2014 version of IFRS 9 introduces an 'expected credit loss' model for the measurement of the impairment of financial assets, so it is no longer necessary for a credit event to have occurred before a credit loss is recognised

Hedge accounting

Introduces a new hedge accounting model that is designed to be more closely aligned with how entities undertake risk management activities when hedging financial and non-financial risk exposures

De-recognition

The requirements for the de-recognition of financial assets and liabilities are carried forward from IAS 39.

The directors of the bank are assessing the impact of the application of IFRS 9 in the future. The adoption of this standard may have an impact on the Bank’s consolidated financial statements in future periods.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(b) Adoption of new and revised International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC) (Continued)

ii) Impact of new and amended standards in issue but not yet effective in the year ended 30 June 2017 (continued)

IFRS 9: Financial Instruments (continued)

Key requirements of IFRS 9: (continued)

IFRS 15: Revenue from Contracts with Customers

In May 2014, IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should 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.

The directors anticipate that the adoption of this standard may not have a significant impact on the Bank’s consolidated financial statements in future periods.

IFRS 16: Leases

IFRS 16 specifies how an IFRS reporter will recognise, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16’s approach to lessor accounting substantially unchanged from its predecessor, IAS 17.

The directors of the bank are assessing the impact of the application of IFRS 16 in the future. The adoption of this standard may have an impact on the Bank’s consolidated financial statements in future periods.

Amendments to IAS 7: Statement of Cash Flows

Amends IAS 7 Statement of Cash Flows to clarify that entities shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities

The directors anticipate that the application of these amendments may not have a significant impact on the Bank’s consolidated financial statements in future periods.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(b) Accounting for currency expenses

The cost of unissued bank note stocks is recognised in the statement of financial position as deferred currency costs under 'other assets'. Bank note costs are charged to profit or loss in the year in which the bank notes are issued.

Coin minting costs are charged to profit or loss when issued to the public. The cost of new currency coins not yet issued is recognised as inventory within 'other assets' consistent with the accounting for the cost of unissued bank note stocks.

(c) Consolidation

Kenya School of Monetary Studies is a subsidiary of the Bank. The Bank has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Bank.

The group uses the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the group. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair value at the acquisition date.

The excess of the aggregate of the consideration transferred and the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the Bank's share of the identifiable net assets acquired is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in profit or loss.

Inter-company transactions, balances and unrealised gains on transactions between group entities are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Bank.

(d) Functional currency and translation of foreign currencies

i. Functional and presentation currency

Items included in the financial are measured using the currency of the primary economic environment in which the Bank operates (the "Functional Currency"). The financial statements are presented in Kenya Shillings ("Shs") which is the Bank's Functional Currency.

ii. Transactions and balances

Foreign currency transactions are translated into the Functional Currency using exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. All foreign exchange gains and losses are presented in profit or loss within 'foreign exchange gains/(losses)'.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(e) Sale and repurchase agreements

Securities sold subject to repurchase agreements ('repos') are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral; the counterparty liability is included in investments by banks.

Securities purchased under agreements to resell ('reverse repos') are recorded as advances to banks. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Securities lent to counterparties are also retained in the financial statements.

The Bank from time to time mops up money from the financial market ('repos') or injects money into the market ('reverse repos') with maturities of 4 - 7 days. The Bank engages in these transactions with commercial banks only. These have been disclosed in the financial statements as 'advances to banks' and 'investments by banks'.

(f) Financial assets and liabilities

i. Financial assets

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity and available-for-sale financial assets. The directors determine the classification of its financial assets at initial recognition. The Bank uses trade date accounting for regular way contracts when recording financial asset transactions.

Financial assets at fair value through profit or loss

This category comprises two sub-categories: financial assets classified as held for trading, and financial assets designated by the Bank as at fair value through profit or loss upon initial recognition.

A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorised as held for trading unless they are designated and effective as hedging instruments. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The Bank designates certain financial assets upon initial recognition as at fair value through profit or loss (fair value option). This designation cannot subsequently be changed and can only be applied when the following conditions are met:

- the application of the fair value option reduces or eliminates an accounting mismatch that would otherwise arise or
- the financial assets are part of a portfolio of financial instruments which is risk managed and reported to senior management on a fair value basis or
- the financial assets consist of debt host and embedded derivatives that must be separated.

Financial instruments included in this category are recognised initially at fair value; transaction costs are taken directly to profit or loss. Gains and losses arising from changes in fair value are included directly in profit or loss and are reported as Fair value loss on financial assets held for trading '. Interest income and expense and dividend income and expenses on financial assets held for trading are included in interest income' and 'interest expense' respectively.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(f) Financial assets and liabilities

i. Financial assets and liabilities (Continued)

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Loans and receivables are initially recognised at fair value – which is the cash consideration to originate or purchase the loan including any transaction costs – and measured subsequently at amortised cost using the effective interest method.

The Bank operates a staff loans scheme for its employees for the provision of facilities such as house and car loans. The loans are granted to staff at an interest rate of 3% per annum which generally below the prevailing market interest rates. Loans issued at non market rates are initially measured at fair value (by discounting the related cash flows using market rates of interest) and subsequently carried at amortised cost. The difference between the fair value of the loans and the carrying amount at inception is treated as a long term employee benefit and is accounted for as a deferred cost. The resulting loan adjustment account is released to interest income over the loan period in line with the unwinding of the discount, while the deferred cost is expensed to staff costs as the services are rendered to the Bank over the period of the loan.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless the investment matures or management intends to dispose of it within 12 months of the end of the reporting period.

Available-for-sale financial assets are measured at fair value. Gains or losses arising from fair value re-measurements are included in other comprehensive income.

ii. Financial liabilities

The Bank's holding in financial liabilities represents mainly deposits from banks and government and other liabilities. Such financial liabilities are initially recognised at fair value and subsequently measured at amortised cost.

Cash Reserve Ratio are statutory deposits taken from commercial banks and non-bank financial institutions for liquidity management as part of monetary policies in accordance with the Kenyan Banking Act and are interest free.

iii. Determination of fair value

For financial instruments traded in active markets, the determination of fair values of financial instruments is based on quoted market prices or dealer price quotations. This includes listed equity securities and quoted debt instruments on major exchanges and broker quotes from Bloomberg.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indicators that a market is inactive are when there is a wide bid-offer spread or significant increase in the bid-offer spread or there are few recent transactions.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(f) Financial assets and liabilities

iii. Determination of fair value (Continued)

For all other financial instruments, fair value is determined using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques, using inputs.

In cases when the fair value of unlisted equity instruments cannot be determined reliably, the instruments are carried at cost less impairment. The fair values of contingent liabilities and irrevocable loan commitments correspond to their carrying amounts.

iv. De-recognition

Financial assets are derecognised when the contractual rights to receive the cash flows from these assets have ceased to exist or the assets have been transferred and substantially all the risks and rewards of ownership of the assets are also transferred (that is, if substantially all the risks and rewards have not been transferred, the Bank tests control to ensure that continuing involvement on the basis of any retained powers of control does not prevent de-recognition). Financial liabilities are derecognised when they have been redeemed or otherwise extinguished.

v. Classes of financial instruments

Category (as defined by IAS 39)		Class (as determined by the Bank)		2017	2016
				Shs' million	Shs' million
Financial assets	Financial assets at fair value through profit or loss	Held for trading	World Bank Reserve Asset Management Programme (RAMP) financial assets	31,789	30,515
			Fixed income securities	102,915	102,662
		Designated at initial recognition	Gold holdings	73	75
	Loans and receivables	Advances to banks		34,870	44,679
		Funds with IMF		1,877	1,923
		Net advances to staff and banks under liquidation		2,575	2,566
		Other assets (classified as financial assets)		12,536	5,837
		Due from Government	Government loan	24,449	25,559
			Overdraft facility to Government	-	44,203
		Balances due from banking institutions	Foreign denominated Term deposits	735,548	696,004
	Available-for-sale	Investment securities	SWIFT shares	9	9
Financial liabilities	Financial liabilities at amortised cost	Deposits from banks	Cash reserve ratio and current account deposits	209,792	218,491
		Due to IMF		115,125	122,438
		Other liabilities		2,559	4,780
		Investment by Banks		-	7,843
		Deposits from Government institutions		253,787	277,481

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(f) Financial assets and liabilities

vi. Impairment of financial assets

a. Loans and receivables

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. If there is objective evidence that an impairment loss on loans carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial instrument's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. A loan is normally written off, either partially or in full, when there is no realistic prospect of recovery of the principal amount, and for a collateralised loan, after taking into account any value of the security which has been realised.

b. Available for sale financial assets

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. If there is objective evidence that an impairment loss, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss.

If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss.

If any such evidence exists for available-for-sale financial assets, impairment losses recognised in profit or loss on equity instruments are not reversed through profit or loss.

v. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(h) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

(i) Property and equipment

Land and buildings comprise mainly branches and offices. All equipment used by the Bank is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Land and buildings are stated at valuation less accumulated depreciation. Valuations are carried out every three years.

Subsequent expenditures are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of the replaced part is de-recognised. All other repair and maintenance costs are charged to profit or loss during the financial period in which they are incurred.
Freehold land is not depreciated. Depreciation of other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(i) Property and equipment (Continued)

Asset classification	Useful life	Depreciation rate
Leasehold land	Over the period of the lease	
Buildings	20 years	5%
Motor vehicles	4 years	20%
Furniture and equipment	5 - 10 years	10-20%

No depreciation is charged on work in progress and assets held in clearing accounts. Depreciation of property and equipment is made from date of placement to use and it ceases when the asset is obsolete, classified as held for sale, fully depreciated or derecognized as per policy.

(j) Intangible assets

Costs associated with maintaining computer software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Bank are recognised as intangible assets when the following criteria are met:

(i.) It is technically feasible to complete the software product so that it will be available for use;
(ii.) Management intends to complete the software product and use or sell it;

- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and

(iii.) The expenditure attributable to the software product during its development can be reliably measured.

Directly attributable costs that are capitalised as part of the software product include the software development employee costs and an appropriate portion of relevant overheads.

Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

Computer software development costs recognised as assets are amortised over their estimated useful lives, which does not exceed three years. Computer software under installation and not yet place in use is held in software clearing account and not amortized until commissioned.

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives. Software has a maximum expected useful life of 5 years.

(k) Impairment of non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset’s carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset’s fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). The impairment test also can be performed on a single asset when the fair value less cost to sell or the value in use can be determined reliably. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (Continued)

(l) Employee benefits

The Bank operates a defined benefit and defined contribution pension schemes. The schemes are funded through payments to trustee-administered funds on a monthly basis.

On the defined contribution scheme, the Bank pays fixed contributions to the scheme. The payments are charged to the profit or loss in the year to which they relate. The Bank has no further payment obligation once the contributions have been paid.

The defined benefit plan defines an amount of pension benefit that an employee will receive on retirement, dependent on age, years of service and compensation.

The assets of the scheme are held by the Bank in an independent trustee administered fund. The asset recognised in the statement of financial position in respect of the defined benefit pension scheme is the fair value of the scheme's assets less the present value of the defined benefit obligation at the reporting date. The defined benefit obligation is calculated annually by an independent actuary using the projected unit method. The present value of the defined benefit obligation is determined by discounting the estimated cash outflows using interest rates of Kenya treasury bonds that have terms to maturity approximating to the terms of the related pension liability.

The asset recognised in the statement of financial position in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash
outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation.

Past-service costs are recognised immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

The Bank and all its employees contribute to the National Social Security Fund, which is a defined contribution scheme.

A defined contribution plan is a retirement benefit plan under which the Bank pays fixed contributions into a separate entity. The Bank has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

The Bank's contributions to the defined contribution scheme are charged to the profit or loss account in the year in which they fall due.

The estimated monetary liability for employees' accrued annual leave entitlement at the reporting date is recognised as an expense accrual.

(m) Income tax

Section 7 of the Income Tax Act exempts the Bank from any taxation imposed by law in respect of income or profits. This exemption includes stamp duty in respect of instruments executed by or on behalf of the Bank.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (continued)

(n) Provisions

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

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

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

(o) Surplus funds

The *Central Bank of Kenya Act (Cap 491)* allows the Bank to retain at least 10% or any other amounts as the board, in consultation with the minister, may determine, off the net annual profit (surplus) of the bank after allowing for the expenses of operations and after provision has been made for bad and doubtful debts, depreciation in assets, contributions to staff benefit funds, and such other contingencies and accounting provisions as the Bank deems appropriate.

(p) Share capital

Ordinary shares are classified as 'share capital' in equity.

(q) Leases

Bank as lessee

The leases entered into by the Bank are primarily operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

Bank as lessor

The group leases certain property, plant and equipment where it does not transfer substantially all the risks and benefits of ownership of the assets. The operating leases generate rental income which is recorded in the income statement on a straight-line basis over the period of the lease.

(r) Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised in profit or loss using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or liability on initial recognition. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument, and any revisions to these estimates are recognised in the income statement. The calculation includes amounts paid or received that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (continued)

(s) Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided.

The Bank earns from the Government of Kenya a commission of 1.5% of amounts raised through its agency role in the issuance of Treasury bills and bonds. The annual commission income is limited to Sh.3 billion as per the agreement between the Bank and the National Treasury effective 1 July 2007. In addition, the Bank earns commissions from other debt instruments issued to meet funding requirements of State Corporations.

(t) Commitments on behalf of the Kenya Government and National Treasury

The Bank issues Treasury bills and bonds on behalf of the National Treasury. Commitments arising on such transactions on behalf of Kenya Government and the National Treasury are not included in these financial statements as the Bank is involved in such transactions only as agent.

(u) Currency in circulation

Notes and coins in circulation are measured at fair value. Currency in circulation represents the nominal value of all bank notes and coins held by the public and commercial banks.

(v) Inventories

The Bank's inventory is comprised of new currency notes issued. Inventories are stated at the sum of the production costs. Cost is determined using the first-in, first-out (FIFO) method.

Bank notes printing expenses and coin minting costs for each denomination which include ordering, printing, minting, freight, insurance and handling costs are initially deferred. Based on the currency issued into circulation, the respective proportional actual costs incurred are released to the profit or loss from the deferred costs account. The deferred amount is recognised as prepayment and represents un-issued bank notes and coins stock.

(w) Loan due from the Government of Kenya

The loan due from the Government of Kenya arose from overdrawn accounts which were converted to a loan with effect from 1 July 1997 after an amendment to the Central Bank of Kenya Act to limit the Bank's lending to Government of Kenya to 5% of Government of Kenya audited revenue.

On 24 July 2007, a deed of guarantee was signed between the Government of Kenya and Central Bank of Kenya in which the Government agreed to repay the loan at Shs 1.11 billion per annum over 32 years at 3% interest per annum. The security held is lien over cash balances, stock, treasury bonds and such other government securities as are specified in Section 46(5) of the Central Bank of Kenya Act.

The loan due from the Government of Kenya is categorised as a loan and receivables and is measured at amortised cost.

Notes to the Financial Statements (continued)

2 Summary of significant accounting policies (continued)

(x) Funds held at/ due to International Monetary Fund (IMF)

Kenya has been a member of the International Monetary Fund (IMF) since 1966. The Bank is the designated depository for the IMF's holdings of Kenya's currency. IMF currency holdings are held in the No. 1 and No. 2 Accounts, which are deposit accounts of the IMF with the Bank.

Borrowings from and repayments to the IMF are denominated in Special Drawing Rights (SDRs). The SDR balances in IMF accounts are translated into Shillings at the prevailing exchange rates and any unrealized gains or losses are accounted for in accordance with accounting policy on foreign currencies.

On a custodial basis, the Bank holds a non-negotiable, non-interest bearing and en cashable on demand security issued by the Treasury in favour of the IMF in its capacity as the IMF's depository. The security issued is in part payment of Kenya's quota of IMF shares.

(y) Comparatives

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

3 Critical accounting estimates and judgements in applying accounting policies

(i) Critical estimates in applying the entity's accounting policies

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

a. *Post-retirement benefits*

Post-retirement benefits are long term liabilities whose value can only be estimated using assumptions about developments over a long period. The Bank has employed actuarial advice in arriving at the figures in the financial statements (Note 17 which includes assumptions). The Board of Directors considers the assumptions used by the actuary in their calculations to be appropriate for this purpose.

b. *Loans and advances*

Critical estimates are made by the management in determining the recoverable amount of impaired loans and receivables.

c. *Fair value of financial assets*

The fair value of financial instruments that are not traded in an active market and off market loans are determined by using valuation techniques.

d. *Property and equipment*

Land and buildings are carried at fair value; representing open market value determined periodically by internal professional valuers.

(ii) Critical judgements in applying the entity's accounting policies

In the process of applying the Bank's accounting policies, management has made judgements in determining:

- the classification of financial assets and leases
- whether assets are impaired.

Notes to the Financial Statements (continued)

4 Interest income

	2017 Shs' million	2016 Shs' million
Financial assets - held to maturity	7,070	4,065
Loans and advances	6,040	10,858
Financial assets at fair value through profit or loss	1,331	1,010
	14,441	15,933

Interest income from loans and advances comprises:

	2017 Shs' million	2016 Shs' million
Due from Government of Kenya – loan	759	794
Due from Government of Kenya - overdraft	1,270	4,077
Staff loans and advances	150	195
Advances to banks	3,411	5,393
Local commercial banks overnight loans	8	61
Other interest income	442	338
	6,040	10,858

5 Interest expense

	2017 Shs' million	2016 Shs' million
Interest on monetary policy issues – investments by banks	1,445	3,819
Interest paid to IMF	273	138
	1,718	3,957

6 Net trading income

	2017 Shs' million	2016 Shs' million
Net gain on sale of foreign exchange currencies	4,298	6,496
Net loss on held for trading financial assets	(105)	(50)
	4,193	6,446

7 Other income

	2017 Shs' million	2016 Shs' million
Licence fees from commercial banks and foreign exchange bureau	292	250
Penalties from commercial banks and foreign exchange bureau	30	40
Rent income from Thomas De La Rue Kenya Limited	2	2
Kenya School of Monetary Studies operating income - hospitality services and tuition fee	379	217
Gain on disposal of property and equipment	1	4
Miscellaneous income	410	23
	1,114	536

Notes to the Financial Statements (continued)

8 Operating expenses

	2017 Shs' million	2016 Shs' million
Employee benefits (Note 9)	3,468	2,122
Currency production expenses	2,352	1,880
Property maintenance and utility expenses	1,135	834
Depreciation (Note 18)	1,016	946
Amortisation (Note 19)	116	287
Provision for impairment loss on other assets (Note 16)	18	13
Auditor's remuneration	10	10
Transport and travelling	168	176
Office expenses	313	245
Postal service expense	165	120
Legal and professional fees	374	48
Other administrative expenses including KSMS	2,002	1,410
	11,137	8,091

9 Employee benefits

	2017 Shs' million	2016 Shs' million
Wages and salaries	3,663	3,390
Medical expenses	286	330
Other staff costs	300	210
Directors' emoluments (Note 28)	51	27
Net income relating to the retirement benefit asset (Note 17)	(832)	(1,835)
	3,468	2,122

10 Balances due from banking institutions

	2017 Shs' million	2016 Shs' million
Current accounts	25,184	69,108
Foreign currency denominated term deposits(cash & cash equivalents)	489,877	266,363
Accrued interest on term deposits	1,561	1,060
Special project accounts	21,180	16,693
Domestic foreign currency cheque clearing	20,827	15,413
Repos clearing and regional central banks	168	101
Cash and cash equivalents (note 27)	558,797	368,738
Foreign currency denominated term deposits (Long term)	176,751	327,266
	735,548	696,004

Special project accounts relate to amounts received by the Government of Kenya (or its ministries) for specific projects or purposes. An equal and corresponding liability is recorded and disclosed under "Deposits from banks and government (note 22)". The movement in the year is mainly attributable to the proceeds from sponsors of various government projects. This has corresponding transaction leg on the growth of foreign reserves during the year.

Notes to the Financial Statements (continued)

11 Financial assets at fair value through profit or loss

	2017 Shs' million	2016 Shs' million
a. Designated at initial recognition		
Gold holdings	73	75

Movements in gold holdings are due to mark to market movements.

	2017 Shs' million	2016 Shs' million
b. Held for trading		
Fixed income securities	102,915	102,663
Fixed income securities under World Bank RAMP	31,789	30,515
	134,704	133,178
	134,777	133,253

12 Investments securities – Available-for-sale

	2017 Shs' million	2016 Shs' million
Unlisted equity securities	9	9
At start of year	9	9
Additions	-	-
At end of year	9	9

"Unlisted equity securities" relate to the Bank's investment in shares of the Society for Worldwide Interbank Financial Telecommunication (SWIFT) which member is owned co-operative with its headquarters in Belgium. The Bank held 24 (2016: 24) SWIFT shares at 30 June 2017.

13 Funds held at/ due to International Monetary Fund (IMF)

	2017 SDR million	2017 Shs' million	2016 SDR million	2016 Shs' million
(a) Assets				
IMF balances (SDR asset account)	13	1,877	14	1,923
(b) Liabilities				
International Monetary Fund Account No. 1	20	2,786	20	2,837
International Monetary Fund Account No. 2	-	12	-	-
International Monetary Fund – PRGF Account	520	74,916	588	82,995
IMF - SDR Allocation account	260	37,411	260	36,606
	800	115,125	868	122,438

The SDR assets account represents the Bank's current account with the IMF while, the liabilities Accounts 1 and 2 are IMF Kenya office balances deposited with the Bank. The PRGF and the SDR Allocation accounts are loans advanced to the Bank by the IMF.

Notes to the Financial Statements (continued)

13 Funds held at/ due to International Monetary Fund (IMF) (Continued)

The National Treasury is the Government of Kenya's Fiscal Agent. Commitments arising on transactions between IMF, Kenya Government and the National Treasury are not included in these financial statements as the Bank is not the Government's fiscal agent.

Kenya's quota in IMF of SDR 271.4 million (2016: SDR 271.4 million) are not included in the financial statements of the Bank as these are booked in the National Treasury with the Government of Kenya's Fiscal Agent and allocations of SDR 260 million (2016: 258.3 million) are included in the financial statements of the Bank as custodian.

14 Securities and advances to banks

	2017 Shs' million	2016 Shs' million
Treasury bonds discounted	10,918	2,629
Treasury bills discounted	36	6,751
Accrued interest Bonds Discounted	316	96
Repo Treasury Bills(Injection)	14,641	28,592
Accrued interest Repo	22	114
Liquidity Support framework	7,530	6,497
Due from Commercial banks	1,407	-
	34,870	44,679

As at 30 June 2017

Advances to Banks Analysis	1-3 months Shs' million	Maturity period 3-12 months Shs' million	Over 1 year Shs' million	Total Shs' million
Treasury bills discounted	-	36	-	36
Treasury bonds discounted		1,560	9,358	10,918
Accrued interest Bonds Discounted	-	316	-	316
Repo Treasury Bills & Bonds (Injection)	14,641	-	-	14,641
Accrued interest Repo	22	-	-	22
Due from Commercial banks	1,407	-	-	1,407
Liquidity Support framework	7,530	-		7,530
	23,600	**1,912**	**9,358**	**34,870**

At 30 June 2016

Treasury bonds discounted	-	1,467	1,162	2,629
Treasury bills discounted	6,714	37	-	6,751
Accrued interest Bonds Discounted	-	96	-	96
Repo Treasury Bills(Injection)	28,592	-	-	28,592
Accrued interest Repo	114	-	-	114
Liquidity Support framework	6,497	-	-	6,497
	41,917	**1,600**	**1,162**	**44,679**

Financial sector have since stabilized and the industry is in sound footing.

Notes to the Financial Statements (continued)

15 Loans and advances

	2017 Shs' million	2016 Shs' million
Due from banks under liquidation	3,400	3,656
Advances to employees	2,643	2,657
	6,043	6,314
Allowance for impairment	(3,468)	(3,747)
Net advances	2,575	2,566
Movement in the loan impairment allowance is as follows:		
At start of year	3,747	3,688
(Decrease)/Increase in impairment allowance	(24)	59
Recoveries collected in the year	(255)	-
At end of year	3,468	3,747

16 Other assets

	2017 Shs' million	2016 Shs' million
Prepayments	319	889
Impersonal accounts	6,598	-
Deferred currency expenses	2,401	2,078
Sundry debtors	5,938	5,837
Items in the course of collection	181	297
Uncleared effects	43	80
	15,480	9,181
Provision for impairment	(4,914)	(4,896)
	10,566	4,285

All other assets balances are recoverable within one year.

	2017	2016
Movement in the impairment allowance is as follows:		
At start of year	4,896	4,883
Increase in impairment allowance	18	13
At end of year	4,914	4,896

Notes to the Financial Statements (continued)

17 Retirement benefit asset

	2017 Shs' million	2016 Shs' million
Present value of funded obligations	13,440	17,623
Fair value of plan assets	(28,464)	(27,161)
Net overfunding in funded plan	(15,024)	(9,538)
Limit on defined benefit asset	6,827	1,762
Asset in the statement of financial position	(8,197)	(7,776)
Movements in the net defined benefit asset recognised are as follows:		
At start of year	7,776	4,668
Net income recognised in the income statement	832	1,835
Net income/(expense) recognized in other comprehensive income	(512)	1,174
Employer contributions	101	99
At end of year	8,197	7,776
Movements in the plan assets are as follows:		
At start of year	27,161	27,156
Expected return on scheme assets	3,544	3,646
Actuarial (loss)/gain	-	(3,517)
Employer contributions	101	99
Employee contributions	51	48
Benefits expenses paid	(983)	(1,119)
Adjustment for previous year values	(1,410)	848
At end of year	28,464	27,161
Movements in the plan benefit obligation are as follows:		
At start of year	17,623	17,820
Current service cost net of employees' contributions	193	347
Interest cost	2,286	2,313
Employee contributions	50	49
Actuarial loss due to experience	(3,078)	(1,787)
Acturial loss due to change in assumptions	(2,651)	-
Benefits paid	(983)	(1,119)
At end of year	13,440	17,623

The principal actuarial assumptions at the reporting date were:	2017	2016
Discount rate (p.a.)	13.9%	13.3%
Salary increase (p.a.)	7.0%	11.3%
Expected return on plan assets (p.a.)	12.9%	12.9%
Future pension increases	3.0%	3.0%

Notes to the Financial Statements (continued)

17 Retirement benefit asset (Continued)

Five year summary	2017 Shs' million	2016 Shs' million	2015 Shs' million	2014 Shs' million	2013 Shs' million
Fair value of plan assets	28,464	27,161	27,156	24,665	21,173
Present value of funded obligations	(13,440)	(17,623)	(17,820)	(17,006)	(13,065)
Adjustment to retirement benefit	(6,827)	(1,762)	(4,668)	-	-
Net retirement benefit asset	8,197	7,776	4,668	7,659	8,108

Plan assets are distributed as follows:

	2017 Shs' million	2017 %	2016 Shs' million	2016 %
Quoted shares	7,977	28%	9,268	34%
Investment properties	6,336	22.3%	5,477	20%
Government of Kenya treasury bills and bonds	9,963	35.0%	9,672	36%
Commercial paper and corporate bonds	1,608	5.6%	1,760	6%
Offshore investments	208	0.7%	-	-
Fixed and term deposits	2,055	7.2%	603	2%
Net current assets	317	1.1%	381	1%
	28,464	100%	27,161	100%

Sensitivity of principal actuarial assumptions:

If the discount rate is 1% higher (lower), the present value of funded obligations would decrease by Shs 1,438 million (increase by Shs 1,438 million). This sensitivity analysis has been determined based on reasonably possible changes of the assumption occurring at the end of the reporting period, while holding all other assumptions constant.

Notes to the Financial Statements (continued)

18 Property and equipment

	Freehold land and Buildings Shs' million	Leasehold land and buildings Shs' million	Work in progress Shs' million	Motor vehicles Shs' million	Furniture and equipment Shs' million	Total Shs' million
Year ended 30 June 2016						
Opening net amount	10,529	2,203	5,918	88	2,005	20,743
Additions	1,962	-	413	25	192	2,592
Disposals-NBV	-	-	-	(3)	(1)	(4)
Charge for the year	(421)	(46)	-	(53)	(426)	(946)
At end of year	12,070	2,157	6,331	57	1,770	22,385
At 30 June 2016						
Cost	12,491	2,203	6,331	388	4,435	25,848
Accumulated depreciation	(421)	(46)	-	(331)	(2,665)	(3,463)
Net book amount	12,070	2,157	6,331	57	1,770	22,385
Year ended 30 June 2017						
Opening net amount	12,070	2,157	6,331	57	1,770	22,385
Additions	-	-	1,044	-	229	1,273
Transfer	-	-	(86)	-	86	-
Reclassification-Cost	-	-	-	-	64	64
Reclassification-Depreciation	-	-	-	-	(1)	(1)
Disposals-NBV	-	-	-	-	(2)	(2)
Charge for the year	(480)	(50)	-	(18)	(468)	(1,016)
At end of year	11,590	2,107	7,289	39	1,678	22,703
At 30 June 2017						
Cost	12,492	2,203	7,289	388	4,794	27,166
Accumulated depreciation	(902)	(96)	-	(349)	(3,116)	(4,463)
Net book amount	11,590	2,107	7,289	39	1,678	22,703

Notes to the Financial Statements (continued)

18 Property and equipment (continued)

Land and buildings were revalued by internal professional valuers in 2015 on an open market basis and the revaluation has been included in the revaluation reserve. Land and buildings are included in the level 2 of the fair valuation hierarchy (that is, the fair value is based on inputs other than quoted prices that are observable).

The methods and significant assumptions applied in arriving at the revalued amounts are as follows:

- The Bank's residential properties are all owner-occupied. In carrying out the valuation, the Bank has assumed that the prospective rental income to be generated by the property based on the going rentals for similar properties within the same location.
- The Bank has taken into account comparable values of similar properties (plot, construction standards, design, lay out, size, location, current sale prices of vacant plots and those developed) to derive the market prices. These were obtained from market transactions of comparable properties.

The Bank is in possession of all titles deeds and occupies all the properties.

19 Intangible assets

Year ended 30 June 2016	Software Shs' Million	Work-in-Progress Shs' Million	Total Shs' Million
Year ended 30 June 2016			
Cost			
At start of year	1,723	2	1,725
Disposals	(4)	-	(4)
Transfers	2	(2)	-
At end of year	1,721	-	1,721
Accumulated amortisation			
At start of year	1,231	-	1,231
Elimation on disposal	(4)	-	(4)
Amortisation for the year	287	-	287
At end of year	1,514	-	1,514
Net carrying value	207	-	207
Year ended June 30 2017			
Cost			
At start of year	1,721	-	1,721
Additions	24	-	24
Reclassification	(64)	-	(64)
At end of year	1,681	-	1,681
Accumulated amortisation			
At start of year	1,514	-	1,514
Reclassification	(1)	-	(1)
Amortisation for the year	116	-	116
At end of year	1,629	-	1,629
Net carrying value	52	-	52

Notes to the Financial Statements (continued)

20 Due from Government of Kenya

	2017 Shs' million	2016 Shs' million
Overdraft	-	44,203
Government loan	24,449	25,559
	24,449	69,762

The Government of Kenya overdraft account is used to fund the treasury bills and interest related accounts that overdraw as a result of shortfalls from primary issues in the market. Whenever the previously funded account receives funding as a result of proceeds from primary issues of call-ups, the overdraft account is refunded the previously owed amount. The overdraft facility had been fully refunded at the close of the year.

Section 46(3) of the *Central Bank of Kenya Act* sets the limit of the Government of Kenya's overdraft facility at the Bank at 5% of the Gross Recurrent Revenue as reported in the latest Government of Kenya audited financial statements. The limit for the year ending 30 June 2017 is Shs.52,102 million (2016: Shs.46,813 million) based on the gross recurrent revenue for the year ended 30 June 2015, which are the latest audited financial statements at the date of approval of these financial statements. Interest is charged at the Central Bank Rate currently at 10%.

The Bank converted the Government of Kenya overdraft facility (Shs.35,600 million) that exceeded statutory limit in 1997 into a loan at 3% interest repayable by 2039 and is guaranteed by a deed executed by the Minister of Finance. Principal repayments of Shs.555 million plus interest accruing are paid half yearly. The movement in the balance in the current year includes the year repayment of principal of Shs.1,110 million which was received by 30 June, 2017.

21 Currency in circulation

	2017 Shs' million	2016 Shs' million
Kenya bank notes	245,595	227,192
Kenya coins	8,192	7,559
	253,787	234,751
Movement in the account was as follows:		
At start of year	234,751	222,178
Deposits by commercial banks	(513,252)	(513,086)
Withdrawals by commercial banks	532,179	525,568
Withdrawals by CBK	109	91
At end of year	253,787	234,751

22 Deposits from banks and government

	2017	2016
Local commercial banks clearing accounts and cash ratio reserve	145,815	179,835
Local banks foreign exchange settlement accounts	28,526	14,133
External banks foreign exchange settlement accounts	179	36
Other public entities and project accounts	35,272	24,559
Government of Kenya	260,317	277,481
	470,109	496,044

Notes to the Financial Statements (continued)

23 Liquidity deposits

	2017 Shs' million	2016 Shs' million
Liquidity deposits	-	7,843
	-	7,843

Liquidity deposits relates to amounts arising from mopping up of excess liquidity in the market. This is managed through selling of repurchase agreements ('repos') to commercial banks .The liquidity deposits matured and they were paid in full.

24 Other liabilities

	2017 Shs' million	2016 Shs' million
Impersonal accounts	-	1,399
Sundry creditors	2,106	2,402
Refundable deposits	243	797
Leave accrual	156	126
Gratuity to staff members	54	56
	2,559	4,780

Impersonal accounts are accounts to which the Bank posts amounts from the National Treasury temporarily pending allocation to a Government of Kenya Ministry.

25(a) Share capital

	Authorised share capital Shs' million	Authorised share capital Shs' million
Balance at 1 July 2015, 30 June 2016 and 30 June 2017	5,000	5,000

Ownership of the entire share capital is vested in the Principal Secretary to the National Treasury.

25(b) General reserve fund

The general reserve fund represents accumulated surpluses comprising surplus arising from normal operations of the Bank and unrealized gains on exchange rates fluctuations. The distribution of these amounts is subject to the Bank retaining at least 10% of annual surplus for the year or any other amount as the Board in consultation with the Minister may determine.

25(c) Revaluation reserve

The revaluation reserve relates to unrealized gains on valuation of land and buildings that will not be recycled into profit or loss. The reserve is non-distributable.

Notes to the Financial Statements (continued)

26 Cash generated from operations

	2017 Shs' million	2016 Shs' million
Reconciliation of net surplus to cash flows from operations:		
(Deficit)/surplus for the year	17,562	(5,814)
Adjustments for:		
Depreciation (Note 18)	1,016	946
Amortisation (Note 19)	116	287
Gain on disposal of property and equipment (Note 7)	(1)	(4)
Net credit relating to the retirement benefit asset (Note 17)	(832)	(1,835)
Employer contributions on defined benefits scheme	(101)	(99)
Changes in working capital:		
Loans and advances	(9)	(233)
Other assets	(6,281)	246
Due from Government of Kenya	45,313	(6,599)
Currency in circulation	19,036	12,573
Deposits	(25,935)	164,728
Other liabilities	(2,221)	313
Investments by banks	(7,843)	7,843
Net cash generated from operations	39,820	172,352

27 Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents include:

	2017 Shs' million	2016 Shs' million
Balances due from banking institutions (Note 10)	558,797	368,738
Financial assets - FVPL (Note 29 ii)	1,998	10,938
Securities discounted by banks and other advances (Note 14)	23,600	41,917
	584,395	421,593

Notes to the Financial Statements (continued)

28 Related party transactions

In the course of its operations, the Bank enters into transactions with related parties, which include the Government of Kenya (the ultimate owner of the Bank) and the Kenya Deposit Insurance Corporation (formerly, the Deposit Protection Fund Board) which is established by law as a deposit insurance scheme to provide cover for depositors and act as a liquidator of failed member institution. It is managed by a Board including the Governor of the Central Bank of Kenya.

The main transactions are ordinary banking facilities to government ministries included in Note 22 and lending to the Government of Kenya included in Note 20.

(i) Loans

The Bank extends loan facilities to the key management staff of the Central Bank. The advances are at preferential rates of interest determined by the Bank.

	2017 Shs' million	2016 Shs' million
Loans to key management staff		
At start of the year	52	60
Loans advanced during the year	16	8
Loan repayments	(24)	(16)
At end of the year	44	52

(ii) Directors' emoluments:

Fees to non-executive directors	13	6
Directors travelling expenses	4	-
Other remuneration to executive director	34	21
	51	27

(iii) Remuneration to senior management	165	181
(iv) Post–employment pension to senior management	4	12

(v) Government of Kenya

	2017 Shs' million	2016 Shs' million
Due from Government of Kenya (Note 20)	24,449	69,762
Government of Kenya Deposits (Note 22)	260,317	277,481
Interest earned from Government of Kenya –Loan (Note 4)	759	794
Interest earned from Government of Kenya-Overdraft (Note 4)	1,270	4,077
Loans Principal repayment	1,110	1,110

Notes to the Financial Statements (continued)

28 Related party transactions (continued)

(v) Government of Kenya (Continued)

Transactions entered into with the Government include:

i. Banking services;
ii. Management of issue and redemption of securities at a commission and;
iii. Foreign currency denominated debt settlement and other remittances at a fee.

(vi) Kenya Deposit Insurance Corporation (KDIC)

The Bank has a close working relationship with the KDIC, an entity incorporated under an Act of Parliament, and provides it with staff and office accommodation. Certain costs incurred on behalf of the KDIC are fully reimbursed to the Bank.

The balance outstanding from the KDIC has been included in sundry debtors (note 16) as at year end was Shs.20.5 million (2016: Shs. 2.4 million).

The deposits relating to KDIC has been included in deposits from banks and Government as at year end was Shs. 27 million (2016: Shs. 143 million)

The staffs of the Corporation are contractually employees of Central Bank but seconded to the Corporation. Salaries of these staff are met by the Central Bank and fully reimbursed by the Corporation. In the year, salaries paid to the staff of Corporation by the Central Bank amounted to Shs. 308 million (2016: Shs. 170,747 million)

(vii) Kenya School of Monetary Studies (KSMS)

The Kenya School of Monetary Studies (the "School") is a registered legal entity 99 % owned by the Bank and 1% by the National Treasury has been consolidated in these financial statements.

The permanent staff working at KSMS are employees of CBK. Fixed assets are also wholly owned by the Bank and a letter of support is issued annually to the external auditor of the School as part of the commitment of the Bank for going concern purposes.

During the year under review, the school's physical developments projects continued as planned with significant percentage of completion recorded. The completed projects include the school's library and Academic block which are now in use while, the construction of the hostels and a new restaurant is on schedule and expected to be completed during next financial year.

(vii) Kenya School of Monetary Studies (KSMS)

	2017 Shs' million	2016 Shs' million
CBK-KSMS related activities		
Grants from CBK	506	465
Buildings	3,223	3,223
Land	4,800	4,800
Deficit	-	(47)
Receivable from KSMS	58	58
Accumulated deficit	20	81

(viii) Central Bank of Kenya Pension Fund and Banki Kuu Pension Scheme 2012

The pension schemes (that is, the defined benefit and defined contribution schemes) are managed and administered by the Secretariat appointed by the sponsor.

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies

The Group's activities expose it to a variety of financial risks, including credit risk and the effects of changes in debt and equity market prices, foreign currency exchange rates and interest rates. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on its financial performance.

Risk management is carried out by the Banking department under policies approved by the Board of Directors. Other organs that monitor the assessment and management of risks within the Bank include: Board Audit Committee, Internal Audit Department and Risk Management Unit.

(a) Strategy in using financial instruments

The Bank holds foreign exchange reserves for the purposes of servicing official foreign debt, paying non-debt government and Central Bank of Kenya expenditures abroad, and occasional intervention in the foreign exchange market to smoothen exchange rate volatilities. The Bank can only intervene in the foreign exchange market when there are sharp exchange rate movements which are likely to destabilize the financial market.

Governed by the Bank's reserve management policy of safe investment, liquidity and return, respectively, the Bank, with a prudent approach, subjects its foreign exchange reserves to investments in international markets.

In this framework, almost all the financial risks to which the Bank is exposed arise while fulfilling its duties of managing foreign exchange reserves and rendering certain banking services to the banking sector and the Government of the Republic of Kenya.

The Bank is exposed to credit, market and liquidity risks due to the aforementioned operations. The financial risks that arise during the management of foreign exchange reserves are the outcome of an investment choice. Nevertheless, the Bank endeavours to minimize such risks by managing them with a conservative approach.

Foreign exchange reserves are managed by observing the investment criteria defined in the Bank's Guidelines on Foreign Exchange Reserves Management.

(b) Risks facing the Bank

The following are the main types of risks that the Bank is exposed to in the course of executing its operations:

- Financial risks include:
  - Credit risk
  - Market risk:
- Interest risk
- Foreign currency exchange risk
  - Liquidity risk

- Non-financial risks include:
  - Operational risk
  - Human resource risk
  - Legal risk
  - Reputation risk

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (Continued)

(b) Risks facing the bank (Continued)

(i) Credit risk

Credit risk arises from investment securities, balances due from banking institutions, funds held with IMF, loans and advances as well as other assets. The Bank has no significant concentrations of credit risk except for the lending to the Government of Kenya.

Management of the credit risk is through the choice of depository banks. The Bank's choice of depository banks is confined to top international banks that meet the set eligibility criteria of financial soundness on long-term credit rating (A), short-term credit rating (F1), composite rating and capital adequacy.

The amount that best represents the Group's maximum exposure to credit risk is per the statement of financial position.

The Bank assesses the credit quality of these assets. None of the balances have had their terms renegotiated as a result of non-performance. Management monitors the credit exposure of staff on a continuous basis, taking into account their financial position, past experience and other factors. Net write back of Shs.24 million (2016: Shs.59 million) have been recognised due to impaired balances to related parties.

The following amounts in loans and advances and other assets are neither past due nor impaired or individually impaired. All other financial instruments operate within their contractual terms.

	Neither past due nor impaired 2017 Shs' million	Individually impaired 2017 Shs' million	Neither past due nor impaired 2016 Shs' million	Individually impaired 2016 Shs' million
Balances due from banking Inst	735,548	-	696,004	-
Advances to banks	34,870	-	44,679	-
Investments securities – AFS	9	-	9	-
Funds held with (IMF)	1,877	-	1,923	-
Financial assets at FVPL	134,777	-	133,253	-
Due from Government of Kenya	24,449	-	69,762	-
Advances to employees	2,575	68	2,566	91
Due from banks under liquidation	-	3,400	-	3,656
Other assets	10,566	4,914	4,285	4,896
	944,671	8,382	952,481	8,643
Allowance for impairment				
- other assets (Note 16)	-	(4,914)	-	(4,896)
- loans and advances (Note 15)	-	(3,468)	-	(3,747)
	-	(8,382)	-	(8,643)
	944,671	-	952,481	-

There were no past due but not impaired balances as at 30 June 2017 - (2016: Nil).

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (continued)

(i) Credit risk (continued)

No.	List of Foreign Correspondent Banks - Current Accounts Balances	Type of Institution	Credit Ratings as of 30th June 2017		
			Fitch	S & P	Moody's
1	Reserve Bank of Australia	Central Bank	NR	NR	NR
2	Bank of Canada	Central Bank	NR	NR	NR
3	Schwerizerische National	Central Bank	NR	NR	NR
4	Bank of China	Commercial Bank	A	A	NR
5	Danmarks National Bank	Central Bank	NR	NR	NR
6	Commerz Bank AG***	Commercial Bank	BBB+	A-	Baa1
7	Bank of France***	Central Bank	NR	NR	NR
8	Standard Chartered Bank, Germany	Commercial Bank	A+	BBB+	A2
9	Bank of England	Central Bank	NR	NR	NR
10	Bank of Japan	Central Bank	NR	NR	NR
11	Bank of Tokyo, Mitsubishi	Commercial Bank		A+	A1
12	Svariges Riksbank	Central Bank	NR	NR	NR
13	Central Bank of Uganda	Central Bank	NR	NR	NR
14	J P Morgan Chase, New York	Commercial Bank	A+	A-	A3
15	Citibank Na , New York	Commercial Bank	A	BBB+	Baa1
16	Federal Reserve , New York	Central Bank	NR	NR	NR
17	Bank of New York Mellon	Commercial Bank	AA-	A	A1
18	South African Reserve Bank	Central Bank	NR	NR	NR

Note: '***NR'*** refers to ***No Rating by Credit Rating Agencies. Central banks are not rated.***
*** No longer hold funds

No.	List of Active Depository Banks	Type of Institution	Credit Ratings as of 30th June 2017		
1	AUST AND NZ BANKING GROUP	Commercial Bank	AA-	AA-	Aa3
2	ABN AMRO BANK NV	Commercial Bank	A+	A	A1
3	BANK OF NEW YORK MELLON CORP	Commercial Bank	AA-	A	A1
4	BANK OF MONTREAL	Commercial Bank	AA-	A+	A1
5	BARCLAYS PLC***	Commercial Bank	A	BBB	Baa2
6	BNP PARIBAS	Commercial Bank	A+	A	A1
7	CAN IMPERIAL BK OF COMMERCE	Commercial Bank	AA-	A+	A1
8	COMMERZBANK AG***	Commercial Bank	BBB+	A-	Baa1
9	COMMONWEALTH BANK OF AUSTRAL	Commercial Bank	AA-	AA-	Aa3
10	RABOBANK	Commercial Bank	AA-	A+	Aa2
11	CREDIT AGRICOLE SA	Commercial Bank	A+	A	A1
12	CREDIT SUISSE GROUP AG-REG***	Commercial Bank	A-	BBB+	Baa2
13	DANSKE BANK A/S	Commercial Bank	A	A	A1
14	DZ BANK AG DEUTSCHE ZENTRAL-	Commercial Bank	AA-	AA-	Aa3
15	ING BANK NV	Commercial Bank	A+	A+	A1
16	JPMORGAN CHASE & CO	Commercial Bank	A+	A-	A3
17	LANDESBANK BADEN-WUERTTEMBER	Commercial Bank	A-	NR	A1
18	MIZUHO FINANCIAL GROUP INC***	Commercial Bank	A-	A-	A1
19	NATIONAL AUSTRALIA BANK LTD	Commercial Bank	AA-	AA-	Aa3
20	NORDEA BANK AB	Commercial Bank	AA-	AA-	Aa3
21	SKANDINAVISKA ENSKILDA BAN-A	Commercial Bank	AA-	A+	Aa3
22	SOCIETE GENERALE SA***	Commercial Bank	A	A	A2
23	STANDARD CHARTERED PLC***	Commercial Bank	A+	BBB+	A2
24	SVENSKA HANDELSBANKEN-A SHS	Commercial Bank	AA	AA-	Aa2
25	SWEDBANK AB - A SHARES	Commercial Bank	AA-	AA-	Aa3

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (continued)

i. Market risk

The Group takes on exposure to market risks, which is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, foreign exchange rates and equity prices. The Bank separates exposures to market risk into either trading or non-trading portfolios. Market risks arising from trading and non-trading activities are concentrated in Bank Treasury and are monitored by management with oversight from the Monetary Policy Committee.

Trading portfolios include those positions arising from market-making transactions where the Bank acts as principal with commercial banks or the market.

Non-trading portfolios primarily arise from the interest rate management of the Bank's investment and monetary policy assets and liabilities. Non-trading portfolios also consist of foreign exchange and equity risks arising from the Bank's held-to-maturity and World Bank RAMP financial assets.

Interest rate risk

The Bank's interest rate risk arises from interest bearing investments, loans and advances to commercial banks and investments by banks. Borrowings issued at variable rates expose the Bank to cash flow interest rate risk which is partially offset by cash held at variable rates. Borrowings issued at fixed rates expose the Bank to fair value interest rate risk.

The tables below summarise the Bank's financial assets and liabilities and analyses them into the earlier of contractual maturity or re-pricing.

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (continued)

ii. Market risk (continued)

Interest rate risk (continued)

At 30 June 2017	1 – 3 months Shs' million	3-12 months Shs' million	1 - 5 years Shs' million	Over 5 years Shs' million	Non-interest Bearing Shs' million	Total Shs' million
Assets						
Balances due from banking institutions	489,877	224,491	-	-	21,180	735,548
Securities & advances to banks	23,600	1,912	9,358	-	-	34,870
Financial assets at FVPL	1,998	40,984	91,722	-	73	134,777
Funds held with International Monetary Fund (IMF)	-	-	-	-	1,877	1,877
Investments securities – Available-for-sale	-	-	-	-	9	9
Loans and advances	111	342	1,100	1,022	-	2,575
Other assets	-	-	-	-	10,566	10,566
Due from Government of Kenya	-	1,110	4,440	18,899	-	24,449
Total financial assets	515,586	268,839	106,620	19,921	33,705	944,671
Liabilities						
Deposits from banks and government	-	-	-	-	470,109	470,109
Due to International Monetary Fund (IMF)	-	-	-	-	115,125	115,125
Other liabilities	-	-	-	-	2,559	2,559
Total financial liabilities	-	-	-	-	587,793	587,793
Interest sensitivity gap	515,586	268,839	106,620	19,921	(554,088)	356,878

As at 30 June 2017, increase of 10 basis points would have resulted in a decrease/increase in profit of Shs.91,096 million (2016:Shs 92,361 million)

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (continued)

ii. Market risk (continued)

Interest rate risk (continued)

At 30 June 2016	1 – 3 months Shs' million	3-12 months Shs' million	1 - 5 years Shs' million	Over 5 years Shs' million	Non-interest Bearing Shs' million	Total Shs' million
Assets						
Balances due from banking institutions	368,666	312,605	-	-	14,733	696,004
Securities & advances to banks	41,917	1,600	1,162	-	-	44,679
Financial assets at FVPL	10,938	31,862	90,378	-	75	133,253
Funds held with International Monetary Fund (IMF)	-	-	-	-	1,923	1,923
Investments securities – Available-for-sale	-	-	-	-	9	9
Loans and advances	111	342	1,109	1,004	-	2,566
Other assets	-	-	-	-	4,285	4,285
Due from Government of Kenya	-	45,303	4,440	20,019	-	69,762
Total financial assets	421,632	391,712	97,089	21,023	21,025	952,481
Liabilities						
Deposits from banks and government	-	-	-	-	496,044	496,044
Due to International Monetary Fund (IMF)	-	-	-	-	122,438	122,438
Other liabilities	-	-	-	-	4,780	4,780
Investments by banks	7,843	-	--	-	-	7,843
Total financial liabilities	7.843	-	-	-	623.262	631.105
Interest sensitivity gap	421,632	391,712	97,089	21,023	(602,237)	321,376

As at 30 June 2016, increase of 10 basis points would have resulted in a decrease/increase in profit of Shs 92,361 million (2015: 745 million)

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (continued)

ii. Market risk (continued)

Foreign exchange risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Monetary Policy Committee sets limits on the level of exposure by currency which is monitored daily.

The table below summarises the Bank's exposure to foreign currency exchange rate risk as at 30 June 2017. Included in the table are the Bank's financial instruments categorised by currency:

	USD Shs' million	GBP Shs' million	EUR Shs' million	SDR Shs' million	Others Shs 'million	Total Shs' million
At 30 June 2017						
Assets						
Balances due from banking institutions	501,045	82,272	3,186	-	149,045	735,548
Financial assets at fair value	134,704	-	-	-	73	134,777
Funds held with International Monetary Fund (IMF)	-	-	-	1,877	-	1,877
Total financial assets	635,749	82,272	3,186	1,877	149,118	872,202
Liabilities						
Due to International Monetary Fund (IMF)	-	-	-	115,125	-	115,125
Deposits from banks and government	23,489	2,020	3,017	-	147	28,673
Total financial liabilities	23,489	2,020	3,017	115,125	147	143,798
Net position	612,260	80,252	169	(113,248)	148,971	728,404

Notes to the Financial Statements (continued)

29 Financial risk management objectives and policies (continued)

ii. Market risk (continued)

Foreign exchange risk (continued)

	USD Shs' million	GBP Shs' million	EUR Shs' million	SDR Shs' million	Others Shs 'million	Total Shs' million
At 30 June 2016						
Assets						
Balances due from banking institutions – Local	372,302	162,392	-	-	161,310	696,004
Financial assets at fair value through profit or loss	133,253	-	-	-	-	133,253
Funds held with International Monetary Fund (IMF)	-	-	-	1,923	-	1,923
Total financial assets	505,555	162,392	-	1,923	161,310	831,180
Liabilities						
Due to International Monetary Fund (IMF)	-	-	-	122,438	-	122,438
Deposits from banks and government	35,573	1,652	1,451	-	84	38,760
Total financial liabilities	35,573	1,652	1,451	122,438	84	161,198
Net position	469,982	160,740	(1,451)	(120,615)	161,226	669,982

As at 30 June 2017, if the shilling had weakened/strengthened by 5% against the major currencies with all other variables held constant, the impact on the Bank's profit would have been:

- USD Shs 31,072 million (2016: Shs 23,499 million)
- Euro Shs 8, million (2016: Shs 8,037 million)
- British Pound Shs 4,012 million (2016: Shs 73million)
- SDR Shs 5,662 million (2016: Shs 6,031 million).

Notes (continued)

29 Financial risk management objectives and policies (continued)

iii. Liquidity risk

Prudent liquidity risk management includes maintaining sufficient cash and marketable securities, and the availability of funding from an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, Treasury maintains flexibility in funding by maintaining availability under committed credit lines.

Management monitors rolling forecasts of the Bank's liquidity reserve on the basis of expected cash flow.

The table below analyses the Bank's financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the statement of financial position date to the contractual maturity date. The amounts disclosed in the table below are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

	On demand Shs' million	1 – 3 months Shs' million	3-12 months Shs' million	1 - 5 years Shs' million	Over 5 years Shs' million	Total Shs' million
At 30 June 2017						
Currency in circulation	-	-	-	-	253,787	253,787
Deposits from banks and government	434,837	-	35,272	-	-	470,109
Due to International Monetary Fund (IMF)	-	-	-	-	115,125	115,125
Other liabilities	-	-	2,559	-	-	2,559
Total financial liabilities	434,837	-	37,831	-	368,912	841,580
At 30 June 2016						
Currency in circulation	-	-	-	-	234,751	234,751
Deposits from banks and government	473,852	-	22,192	-	-	496,044
Due to International Monetary Fund (IMF)	-	-	-	-	122,438	122,438
Other liabilities	-	-	4,780	-	-	4,780
Repo sold to Banks	-	7,843	-	-	-	7,843
Total financial liabilities	473,852	7,843	26,972	-	357,189	865,856

Notes (continued)

29 Financial risk management objectives and policies (continued)

Fair value of financial instruments

IFRS 7 specifies a fair value hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges (for example, Bloomberg).
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). The sources of input parameters like LIBOR yield curve or counterparty credit risk are Bloomberg.
- Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components.

	Level 1 Shs' million	Level 2 Shs' million	Level 3 Shs' million	Total Shs' million
At 30 June 2017:				
Financial assets at fair value	134,704	73	-	134,777
Investment securities – Available-for-sale	-	-	9	9
Total assets	134,704	73	9	134,786
As at 30 June 2016:				
Financial assets at fair value	133,178	75	-	133,253
Investment securities – Available-for-sale	-	-	9	9
Total assets	133,178	75	9	133,262

There were no changes in level 3 instrument as disclosed in Note 12 of the financial statements.

30 Contingent liabilities and commitments

The Bank is party to various legal proceedings. Based on legal advice, the directors believe that no loss will arise from these legal proceedings. Appropriate provisions have been made where a liability is considered probable.

At 30 June 2017, the Bank had capital commitments of Shs.1,979 (2016: Shs.2,059 million) in respect of property and equipment purchases.

Operating lease commitments – Bank as lessee

	2017 Shs' million	2016 Shs' million
Not later than 1 year	164	151
Later than 1 year and not later than 5 years	483	176
	647	327

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