

1 SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements as set out below have been applied consistently to all periods presented in the financial statements.

(a) Revenue recognition

Revenue is derived substantially from banking business and related activities and comprises net interest income and non-interest income. Income is recognised on an accrual basis in the period in which it accrues.

(i) *Net interest income*

Interest income and expenses are recognised in profit or loss for all interest-bearing instruments on an accrual basis using the effective interest method. The effective interest rate is the rate that exactly discounts the expected estimated future cash payments and receipts through the expected life of the financial asset or liability. Where financial assets have been impaired, interest income continues to be recognised on the impaired value, based on the original effective interest rate. External expenses incurred directly as a result of bringing margin-yielding assets on-balance sheet are amortised through interest income over the life of the asset.

(ii) *Fees and commission income*

Fees and commission income is generally recognised when the related services are provided or on execution of a significant act. Fees charged for servicing a loan are recognised as revenue as the service is provided.

(iii) *Net income from other financial instruments at fair value*

Net income from other financial instruments at fair value relates to derivatives held for risk management purposes and includes all realised and unrealised fair value changes and foreign exchange differences.

(b) Financial assets and financial liabilities

(i) *Classification*

Financial assets

Management determines the appropriate classification of financial instruments at the time of the purchase and revalues its portfolio on a regular basis to ensure that all financial assets are appropriately classified. The bank's investments are categorized as:

- *Financial instruments at fair value through profit or loss* – These include financial instruments designated at fair value through profit or loss at inception and those designated as held for trading. A financial instrument is classified in this category if acquired principally for the purpose of selling or repurchasing it in the short term or if so designated by management.
- *Loans and receivables* – These are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the bank provides money directly to a debtor with no intention of trading the receivable. These include advances to customers and placements with other banks.
- *Held-to-maturity investments* – These are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. Were the Bank to sell other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available for sale. These include treasury bills and treasury bonds.
- *Available-for-sale* – These are investments intended to be held to maturity, which may be sold in response to needs for liquidity or changes in interest rates or exchange rates. These include treasury bills and bonds and corporate bonds.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Financial assets and financial liabilities (continued)

(i) Classification (continued)

Financial Liabilities

The bank classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised cost or fair value through profit or loss.

(ii) Recognition

Purchases and sales of financial instruments at fair value through profit or loss and available for sale assets are recognised on the date they are transferred to the Bank.

Loans and receivables are recognised when cash is advanced to the borrowers.

(iii) Measurement

Financial instruments are initially recognised at fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue thereof.

Available-for-sale financial assets and financial instruments at fair value through profit or loss are subsequently carried at fair value. Gains and losses arising from changes in the fair value of the 'financial instruments at fair value through profit or loss' category are included in the profit or loss in the period in which they arise.

Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised in other comprehensive income (OCI), until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in other comprehensive income should be recognised in profit or loss. However, interest calculated using the effective interest method is recognised in the profit or loss.

Loans and receivables are carried at amortised cost using the effective interest method.

(iv) Derecognition

The bank derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the bank is recognised as a separate asset or liability.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the bank is recognised as a separate asset or liability.

The bank enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the statement of financial position. Transfers of assets with retention of all or substantially all risks and rewards include, for example, securities lending and repurchase transactions.

The bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Financial assets and financial liabilities (continued)

(v) *Fair value measurement principles*

Policy applicable from 1 January 2013

‘Fair value’ is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the bank measures assets and long positions at a bid price and liabilities and short positions at an ask price.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the bank on the basis of the net exposure to either market or credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for a particular risk exposure. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Policy applicable before 1 January 2013

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s length transaction on the measurement date. When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on arm’s length basis.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Financial assets and financial liabilities (continued)

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

At each reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset than can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include:

- default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would otherwise consider;
- indications that a borrower or issuer will enter bankruptcy;
- the disappearance of an active market for a security; or
- other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

The Bank considers evidence of impairment at both a specific asset and collective level for loans and receivables and held-to-maturity investments carried at amortised cost. All individually significant loans and receivables and held-to-maturity investments are assessed for specific impairment. Those that are not found to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables and held-to-maturity investments that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortised cost) with similar risk characteristics.

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

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

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale investment securities are recognised by transferring the difference between the amortised acquisition cost and current fair value from equity to profit or loss. When a subsequent event causes the amount of impairment loss on an available-for-sale debt security to decrease, the impairment loss is reversed through profit or loss.

(vii) *Statutory credit risk reserve*

Where impairment losses required by regulations exceed those computed under IFRS, the excess is recognised as a statutory credit risk reserve and is accounted for as an appropriation of retained earnings. The statutory credit risk reserve is non-distributable.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) Cash and cash equivalents

For the purpose of presentation in the statement of cash flows, the cash and cash equivalents include balances with the Central Bank of Kenya which are available to finance the bank's day to day operations, net balances from banking institutions, and investments with maturities of three months or less from the date of acquisition.

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

(d) Derivative financial instruments

The bank enters into financial instruments for trading purposes with third parties to hedge their exposure to foreign exchange and interest rate risks arising from operational, financing and investment activities.

Derivative financial instruments are recognised initially at cost. Subsequent to initial recognition, derivative financial instruments are measured at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions and valuation techniques. The gain or loss on re-measurement to fair value is recognised immediately in profit or loss. The main derivative financial instruments in use by the bank are as follows:

Currency forwards

Foreign exchange forward contracts are agreements to buy and sell a specified quantity of foreign currency, usually on a specified future date at an agreed rate. The fair value of forward exchange contracts is the present value of the mark to market adjustment at the reporting date.

Currency options

A currency option is an agreement between two counter-parties, giving the option buyer (option holder) the right, but not the obligation, either to buy or to sell a quantity of currency at a specified rate, on or before a specified date in the future. All currency options concluded with third parties are immediately offset by an opposite option transacted with another Citibank affiliate under exactly the same parameters (date, notional amount, currency and strike price). The bank receives a premium for the transaction. Thus no fair value of outstanding options is carried on the bank's statement of financial position.

(e) Transactions in foreign currencies

Transactions in foreign currencies during the year are converted into Kenya Shillings at the spot exchange rate at the date of the transaction. Foreign currency monetary assets and liabilities are translated at the spot exchange rate at the reporting date other than the forwards contracts which are carried at prevailing forward rates. Non-monetary assets and liabilities denominated in foreign currency are recorded at the spot exchange rate at the transaction date. Resulting exchange differences are recognised in profit or loss for the year.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(f) Employee benefits

(i) *Retirement benefit schemes*

The majority of the bank's employees are eligible for retirement benefits under a defined contribution plan. Contributions to the defined contribution plan are recognised in profit or loss as incurred.

The employees and the Bank also contribute to the NSSF, a national retirement scheme. Contributions are determined by local statutes and the Bank's contributions are recognised in profit or loss in the year to which they relate.

(ii) *Share based payments*

Certain categories of senior management are awarded ordinary shares in Citigroup Inc (the ultimate holding company) based on their performance. The shares vest over a period of four years. The stock awards are recognised in profit or loss, with a corresponding entry to the equity compensation reserve, on the award date at the market value of the shares on the award date. As the awards are categorised as equity-settled, no adjustment is made for fair value changes until the settlement date.

(iii) *Short term benefits*

Short term employee benefits obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expensed in respect of short term cash bonuses to be paid.

(iv) *Termination benefits*

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

(g) Taxation

Income tax expense comprises current tax and deferred tax. Current tax is the expected tax payable on the taxable income for the year, and any adjustment to tax payable in respect of the previous year. It is measured using tax rates enacted or substantively enacted at the reporting date.

Deferred tax is recognised on temporary differences between the carrying amounts for financial reporting purposes and the amounts used for taxation purposes, except differences relating to the initial recognition of assets or liabilities which affect neither accounting nor taxable profit.

Deferred tax is calculated using rates that are expected to be applied on temporary differences when they are reversed, using tax rates currently enacted or substantively enacted at the reporting date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(h) Property and equipment

Items of property and equipment are measured at cost, less accumulated depreciation and impairment losses. Depreciation is charged on the assets on a straight line basis to allocate the cost to their residual values over useful lives estimated as follows:

- Buildings 2% per annum.
- Computer equipment and computer software 20% to 33⅓% per annum.
- Furniture and equipment 10% to 20% per annum.
- Motor vehicles 25% to 29% per annum.

The residual values of the assets are reviewed, and adjusted if appropriate, at each reporting date. Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are recognised in profit or loss in the year in which they arise.

(i) Intangible assets

The costs incurred to acquire and bring to use specific computer software licences are capitalised. The costs are amortised on a straight line basis over the expected useful lives, from the date it is available for use, not exceeding three years.

Computer development costs that are directly associated with the production of identifiable and unique software products that will probably generate economic benefits in excess of its costs are capitalised. The costs are amortised on a straight line basis over the expected useful lives, from the date that it is available for use, not exceeding three years.

Costs associated with maintaining software are recognised as an expense as incurred.

(j) Operating leases

Leases where a significant portion of the risks and rewards of ownership are retained by the lessor, are classified as operating leases. Payments made under operating leases are recognised in profit or loss on a straight-line basis over the period of the lease.

Prepaid operating lease rentals in respect of leasehold land is recognised as an asset and amortised over the lease period.

Assets held under operating leases are classified as operating leases and are not recognised in the statement of financial position.

(k) Contingent liabilities

Letters of credit, acceptances, guarantees and performance bonds are accounted for as contingent liabilities. Estimates of the outcome and the financial effect of contingent liabilities are made by management based on the information available up to the date the financial statements are approved for issue by management. Any expected loss is recognised in profit or loss.

(l) Related parties

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

(m) Provisions

A provision is recognised in the statement of financial position when the Bank has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and the amount can be estimated reliably.

1 SIGNIFICANT ACCOUNTING POLICIES (Continued)

(n) Impairment for non-financial assets

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

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that are largely independent from other assets and groups. Impairment losses are recognised in profit or loss.

(o) New standards and interpretations

The Bank has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of 1 January 2013. The nature and the effects of the changes are explained below.

- *IFRS 13 Fair Value Measurement (Fair value measurements)*
In accordance with the transitional provisions of IFRS 13, the Bank has applied the new definition of fair value, as set out in Note 3(b) (v), prospectively. The change had no significant impact on the measurements of the Bank's assets and liabilities, but the bank has included new disclosures in the financial statements, which are required under IFRS 13. These new disclosure requirements are not included in the comparative information. However, to the extent that disclosures were required by other standards before the effective date of IFRS 13, the Bank has provided the relevant comparative disclosures under those standards.
- *Amendments to IAS 1 – Presentation of Items of Other Comprehensive Income (Presentation of items of OCI)*
As a result of the amendments to IAS 1, the Bank has modified the presentation of items of other comprehensive income (OCI) in its statement of comprehensive income and OCI, to present items that would be reclassified to profit or loss in the future separately from those that would never be.

2 FINANCIAL RISK MANAGEMENT DISCLOSURES

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

Being a branch, the bank does not have a board of directors but a Management Committee which has overall responsibility for the establishment and oversight of the Bank's risk management framework.

2 FINANCIAL RISK MANAGEMENT DISCLOSURES (Continued)

Through its risk management structure, the bank seeks to manage efficiently the core risks; credit, liquidity and market risk, which arise directly through the bank's commercial activities. In addition compliance, regulatory risk and operational risk are normal consequences of any business undertaking.

The Management Committee has established the Asset and Liability Committee (ALCO), Credit Committee and the Business Risk and Controls Committee (BRCC), which are responsible for developing and monitoring the bank's risk management policies in their specified areas.

The bank's risk management policies are established to identify and analyse the risks faced by the bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

(a) Credit risk

Credit risk management

Credit risk is the risk of financial loss arising from an obligor's failure to meet the terms of any contract or to otherwise fail to perform as agreed.

The bank has well documented policies and procedures for managing credit risk. The policies are based on the principles of:

- Management responsibility
- Defined credit approval authorities
- Set standards for risk measurement
- Consistent approach to origination of credit, documentation and problem recognition
- Portfolio management strategies.

The risk that counterparties might default on their obligations is monitored on an ongoing basis.

To manage the level of credit risk, the bank deals with counterparties of good credit standing and for which in its assessment the transactions are appropriate and risks understood by the counterparty.

The bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments.

Allowances for impairment

Loans are designated as impaired and considered non-performing where recognised weakness indicates that full payment of either interest or principal becomes questionable or as soon as payment of interest or principal is 90 days or more overdue. Where any amount is considered uncollectible, an individual impairment provision is raised, being the difference between the loan carrying amount and the present value of estimated future cash flows. In any decision relating to the raising of provisions, the bank attempts to balance economic conditions, local knowledge and experience, and the results of independent asset reviews. Where it is considered that there is no realistic prospect of recovering an element of an account against which an impairment provision has been raised, then that amount will be written off.

2 FINANCIAL RISK MANAGEMENT DISCLOSURES (Continued)

(a) Credit risk (continued)

A portfolio impairment provision is also held to cover the inherent risk of losses, which, although not identified, are known through experience to be present in the loan portfolio. The provision is estimated by using the historical loss rate, the emergence period and the loan's balance of the performing portfolio.

The portfolio impairment provision is set with reference to past experience using loss rates, and judgmental factors such as the economic environment and the trends in key portfolio indicators. The bank exposure to credit risk is analysed as follows:

2014:	Balances due from foreign banks KShs '000	Placement with other banks KShs '000	Available for sale securities KShs '000	Loans and advances KShs '000
Individually impaired assets	-	-	-	438,252
Allowance for impairment	-	-	-	(438,2)
	-	-	-	-
Performing assets	8,606,505	3,396,930	29,254.359	22,944,446
Portfolio impairment provision	-	-	-	(7,241)
	8,606,505	3,396,930	29,254.359	22,937,205
Total	8,606,505	3,396,930	29,254.359	22,937,205
2013:				
Individually impaired assets	-	-	-	436,969
Allowance for impairment	-	-	-	(436,969)
	-	-	-	-
Performing assets	6,395,749	3,978,760	26,977,290	24,219,095
Portfolio impairment provision	-	-	-	(7,242)
	6,395,749	3,978,760	26,977,290	24,211,853
Total	6,395,749	3,978,760	26,977,290	24,211,853

The bank held Government securities worth KShs 749,450,000. (2013-KShs 1,424,800,000) as collateral against some of its loans and advances.

Write-off policy

The bank writes off a loan / security balance (and any related allowances for impairment losses) when the bank determines that the loans / securities are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower financial position such that the borrower can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

2 FINANCIAL RISK MANAGEMENT DISCLOSURES (Continued)

(b) Liquidity risk

Liquidity risk is the risk that the bank will encounter difficulty in meeting obligations from its financial liabilities. The bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the bank's reputation.

Liquidity risk arises in the general funding of the bank's activities and in the management of positions. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate timeframe.

ALCO is responsible for ensuring that the bank manages its liquidity risk and is able to meet all its obligations to make payments as and when they fall due. It also has primary responsibility for compliance with regulations and bank policy and maintaining a liquidity crisis contingency plan.

The bank maintains a portfolio of short term liquid assets, largely made up of short term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained with daily liquidity positions being monitored.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of liquidity risk.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature are important factors in assessing the liquidity of the bank and its exposure to changes in interest rates and exchange rates.

A substantial portion of the bank's assets are funded by customer deposits made up of current and savings accounts and other deposits. These customer deposits, which are widely diversified by type and maturity, represent a stable source of funds. Lending is normally funded by liabilities in the same currency.

The bank also maintains significant levels of marketable securities either for compliance with statutory requirements or as prudential investments of surplus funds.

A key measure of liquidity risk is the ratio of net liquid assets to deposit liabilities. The Central Bank of Kenya requires banks to maintain a statutory minimum ratio of 20% of liquid assets to all its deposit liabilities.

For this purpose, liquid assets comprises cash and balances with Central Bank of Kenya, net balances with financial institutions, treasury bonds and bills and net balances with banks abroad.

Deposit liabilities comprise deposits from customers, other liabilities that have matured or maturing within 91 days.

The liquidity ratios at the reporting date and during the reporting period (based on month end ratios) were as follows:

	2013	2014
At 31 December/March	62.5%	72.7%
Average for the period	76.6%	70.8%
Highest for the period	85.6%	72.7%
Lowest for the period	62.5%	69.5%

2 **FINANCIAL RISK MANAGEMENT DISCLOSURES (Continued)**

(b) **Liquidity risk (continued)**

Residual contractual maturities of financial liabilities:

31 March 2014:

	On Demand	Due within 3	Due between 3	Due between	Total
	KShs '000	months	and 12 months	1 and 5 years	KShs '000
	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Financial liabilities					
Deposits from banks	5,634,533	1,738,000	-	-	7,372,533
Derivative instruments	71,171	-	-	-	71,171
Due to customers	38,672,566	5,971,430	980,803	300	45,625,099
Other liabilities – Items in transit and bills payable	2,311	1,552,419	-	-	1,554,730
	44,380,581	9,261,849	980,803	300	54,623,533

31 December 2013:

	On Demand	Due within 3	Due between 3	Due between	Total
	KShs '000	months	and 12 months	1 and 5 years	KShs '000
	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Financial liabilities					
Deposits from banks	3,672,910	3,493,010	1,739,000	-	8,904,920
Derivative instruments	135,662	-	-	-	135,662
Due to customers	40,452,962	-	2,913,135	447,520	43,813,617
Other liabilities – Items in transit and bills payable	-	740,544	-	-	740,544
	44,261,534	4,233,554	4,652,135	447,520	53,594,743

Customer deposits up to three months represent current, savings and call deposit account balances, which past experience has shown to be stable and of a long term nature.

2 FINANCIAL RISK MANAGEMENT DISCLOSURES (Continued)

(c) Market risk

Market risk is the risk that changes in market prices, such as interest rate and foreign exchange rates will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands.

The Bank is also exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. Currency risk is managed principally through limits set on the level of exposure by currency and in total for both overnight and intra-day positions which are monitored daily.

Overall responsibility for market risk is vested in ALCO.

Sensitivity analysis interest rate risk

The sensitivity analysis on the accrual book is measured by the change in DV01 (Dollar value of 01) that measures the change in value of the accrual portfolio due to a 1 basis point parallel move in the interest rates. At 31 December 2013, a 1 basis point parallel increase in the interest rates with all other variables held constant would have resulted to a pre-tax loss movement of KShs 2,337,180 (2013 – KShs 2,079,603).

2 FINANCIAL RISK MANAGEMENT (Continued)

(c) Market risk (continued)

(i) Interest rate risk

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The table below summarises the exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

31 March 2014	Effective interest rate	Within 3 months	Between 3 and 12 months	Between 1 and 5 years	Non interest bearing	Total
	%	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Financial assets						
Cash and balances with Central Bank	-	-	-	-	4,481,682	4,481,682
Other assets – Items in transit	-		-	-	943,054	943,054
Available for sale securities	11.8%	12,892,665	8,974,512	7,387,182	-	29,254,359
Due from foreign branches	0.1%	8,606,505	-	-	-	8,606,505
Due from other banks	6.9%	3,396,930	-	-	-	3,396,930
Derivative instruments	-	-	-	-	67,522	67,522
Loans and advances to customers (net)	6.5%	18,290,681	952,665	3,693,859	-	22,937,205
Total financial assets		43,186,781	9,927,177	11,081,041	5,492,258	69,687,257
Financial liabilities						
Deposits from banking institutions	0.8%	7,372,533	-	-	-	7,372,533
Derivative instruments	-	-	-	-	71,171	71,171
Customer deposits	4.3%	44,643,996	980,803	300	-	45,625,099
Other liabilities – Items in transit and bills payable	-	-	-	-	1,554,730	1,554,730
Total financial liabilities		52,016,529	980,803	300	1,625,901	54,623,533
Interest rate sensitivity gap		(8,829,748)	8,946,374	11,080,741	3,866,357	15,063,724

2 FINANCIAL RISK MANAGEMENT (Continued)

(c) Market risk (continued)

(i) Interest rate risk (continued)

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The table below summarises the exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

31 December 2013	Effective interest rate	Within 3 months	Between 3 and 12 months	Between 1 and 5 years	Non interest bearing	Total
	%	KShs '000	KShs '000	KShs '000	KShs '000	KShs '000
Financial assets						
Cash and balances with Central Bank	-	-	-	-	5,888,760	5,888,760
Other assets – Items in transit	-	587,385	-	-	-	587,385
Available for sale securities	11.7%	2,852,872	15,935,654	8,188,764	-	26,977,290
Due from foreign branches	0.1%	6,395,749	-	-	-	6,395,749
Due from other banks	7.6%	3,978,760	-	-	-	3,978,760
Derivative instruments	-	-	-	-	43,830	43,830
Loans and advances to customers (net)	8.3%	20,172,495	428,803	3,610,555	-	24,211,853
Total financial assets		33,987,261	16,364,457	11,799,319	5,932,590	68,083,627
Financial liabilities						
Deposits from banking institutions	1.5%	7,165,920	1,739,000	-	-	8,904,920
Derivative instruments	-	-	-	-	135,662	135,662
Customer deposits	4.7%	40,452,962	2,913,135	447,520	-	43,813,617
Other liabilities – Items in transit and bills payable	-	-	740,544	-	-	740,544
Total financial liabilities		47,618,882	5,392,679	447,520	135,662	53,594,743
Interest rate sensitivity gap		(13,631,621)	10,971,778	11,351,799	5,769,928	14,742,834

2 FINANCIAL RISK MANAGEMENT (Continued)

(c) Market risk (continued)

(ii) Currency rate risk

The Bank operates wholly within Kenya and its assets and liabilities are carried in the local currency. The various foreign currencies to which the Bank is exposed at 31 December 2013 are summarised below:

31 March 2014

	USD KShs '000	GBP KShs '000	EURO KShs '000	JPY KShs '000	Others KShs '000	TOTAL KShs '000
Financial assets						
Balance sheet items						
Cash and balances with banks abroad	9,864,977	128,427	1,424,039	32,687	292,761	11,742,891
Loans and advances	6,470,471	388,134	795,362	103,517	28,603	7,786,087
Other foreign assets	1,601,242	564	55,996	606,457	15,071	2,279,330
Off balance sheet items						
Undelivered spot purchases	675,009	-	-	-	-	675,009
Forward purchases	9,062,921	-	518,582	140,474	147,277	9,869,254
Total financial foreign assets	27,674,620	517,125	2,793,979	883,135	483,712	32,352,571
Financial liabilities						
Balance sheet items						
Deposits	20,029,246	498,158	2,161,829	114,915	268,008	23,072,156
Balances due to banks abroad	-	-	-	-	18,728	18,728
Other foreign liabilities	1,463,660	3,069	64,953	606,524	2,682	2,140,888
Foreign loans and advances	90,750	-	-	-	-	90,750
Inter-company/group balances	1,729,001	-	-	-	-	1,729,001
Off balance sheet items						
Undelivered spot sales	-	-	-	-	-	-
Forward sales	3,577,777	-	518,933	140,358	146,432	4,383,500
Total financial foreign liabilities	26,890,434	501,227	2,745,715	861,797	435,850	31,435,023
Net open position	784,186	15,898	48,264	21,338	47,862	917,548
Long/(short)position	784,186	15,898	48,264	21,338	47,862	917,548

2 FINANCIAL RISK MANAGEMENT (Continued)

(c) Market risk (continued)

(ii) Currency rate risk (continued)

• 31 December 2013

	USD KShs '000	GBP KShs '000	EURO KShs '000	JPY KShs '000	Others KShs '000	TOTAL KShs '000
Financial assets						
Balance sheet items						
Cash and balances with banks abroad	8,887,778	45,022	2,208,139	394,813	232,048	11,767,800
Loans and advances	6,539,872	345,534	352,815	3	23,786	7,262,010
Other foreign assets	2,705,409	1,485	12,417	776,026	35,237	3,530,574
Off balance sheet items						
Undelivered spot purchases	180,166	-	-	-	172,750	352,916
Forward purchases	6,462,250	-	436,058	140,185	41,621	7,080,114
Total financial foreign assets	24,775,475	392,041	3,009,429	1,311,027	505,442	29,993,414
Financial liabilities						
Balance sheet items						
Deposits	18,308,291	336,438	2,491,530	385,040	270,341	21,791,640
Balances due to banks abroad	-	52,573	-	-	2,907	55,480
Other foreign liabilities	2,506,880	3,032	20,659	776,042	2,263	3,308,876
Foreign loans and advances	121,660	-	-	-	-	121,660
Inter-company/group balances	1,727,734	-	-	-	-	1,727,734
Off balance sheet items						
Undelivered spot sales	198,858	-	-	-	172,600	371,458
Forward sales	1,915,029	-	436,320	139,806	41,919	2,533,074
Total financial foreign liabilities	24,778,452	392,043	2,948,509	1,300,888	490,030	29,909,922
Net open position	(2,977)	(2)	60,920	10,139	15,412	83,492
Long/(short)position	(2,977)	(2)	60,920	10,139	15,412	83,492

2 FINANCIAL RISK MANAGEMENT (Continued)

(c) Market risk (continued)

Sensitivity analysis foreign currency exchange risk

The bank's assets and liabilities held in foreign currency are bound to be affected by the fluctuations in the foreign exchange rate. The sensitivity analysis on the foreign currency position is measured by the trading (DVO1) that measures the change in value of the position as a result of a 1 percentage point shift (appreciation) in exchange rates. The trading DVO1 for the KES and the USD positions that constitute the significant portion of the statement of financial position is as follows:

	2014	2013
	KShs'000	KShs'000
USD	623,841	(268,103)
EURO	(52,833)	17,114

(a) Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It includes reputation and franchise risk associated with the Bank's business practices or market conduct; and the risk of failing to comply with applicable laws and regulations.

The Bank seeks to ensure that key operational risks are managed in a timely and effective manner through a framework of policies, procedures and tools to identify, assess, monitor, control and report such risks.

Compliance with operational risk policies and procedures is the responsibility of all business managers. The Business Risk and Controls Committee (BRCC) has the overall responsibility for ensuring that an appropriate and robust risk management framework is in place to monitor and manage operational risk.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This is supported by the Risk and Controls Self Assessment Process that assesses the effectiveness of controls over the risks identified.

(b) Capital management

The Central Bank of Kenya sets and monitors capital requirements for all banks.

The objective of the Central Bank of Kenya is to ensure that a bank maintains a level of capital which:

- is adequate to protect its depositors and creditors;
- is commensurate with the risks associated with its activities and profile; and
- promotes public confidence in the bank.

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

2 FINANCIAL RISK MANAGEMENT (Continued)

(e) Capital management (continued)

Capital adequacy and use of regulatory capital are monitored regularly by management employing techniques based on the guidelines developed by the Basel Committee, as implemented by the Central Bank of Kenya for supervisory purposes.

The Central Bank of Kenya requires a bank to maintain at all times:

- a core capital of not less than 8% of total risk weighted assets, plus risk weighted off-balance sheet items;
- a core capital of not less than 8% of its total deposit liabilities;
- a total capital of not less than 12% of its total risk weighted assets, plus risk weighted off-balance sheet items; and
- a capital conservation buffer of 2.5% over and above the above minimum ratios.

This brings the minimum core capital to risk weighted assets and total capital to risk weighted assets to 10.5% and 14.5% respectively. The capital conservation buffer requirements are effective 1 January 2014.

Central Bank of Kenya required the Bank to maintain a minimum core capital of KShs 1 billion as at 31 December 2013. The bank is already compliant with this requirement.

Capital is segregated into core capital (Tier 1) and supplementary capital (Tier 2).

Core capital includes assigned capital, irredeemable preference shares, share premium and retained earnings after deductions for goodwill and intangible assets.

Supplementary capital on the other hand includes 25% of revaluation reserves of property and equipment, subordinated debt not exceeding 50% of core capital and any other approved reserves.

Risk weighted assets are arrived at using a framework of four weights applied to both on-balance sheet and off-balance sheet items to reflect the relative risk of each asset and counterparty.

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

	2014	2013
	KShs '000	KShs '000
Core capital (Tier 1)		
Assigned capital	4,582,975	4,582,975
Retained earnings	<u>11,103,8027</u>	<u>10,847,622</u>
	<u>15,686,802</u>	<u>15,430,597</u>
Supplementary capital (Tier 2)		
Statutory reserve	<u>299,945</u>	<u>355,004</u>
Total capital	<u>15,986,6747</u>	<u>15,785,601</u>
Risk weighted assets		
On-balance sheet	27,361,309	28,976,545
Off-balance sheet	<u>17,036,295</u>	<u>15,623,350</u>
Total risk weighted assets	<u>62,889,446</u>	<u>44,599,896</u>
Deposits from customers	<u>52,997,632</u>	<u>52,718,537</u>

2 FINANCIAL RISK MANAGEMENT (Continued)

(e) Capital management (continued)

Capital ratios	2014	2013
Core capital/total deposit liabilities (CBK minimum 8%)	30%	29%
Core capital /total risk weighted assets (CBK minimum 8%)	25%	35%
Total capital /total risk weighted assets (CBK minimum 12%)	25%	35%

3 ASSUMPTIONS AND ESTIMATION UNCERTAINTIES

(i) *Impairment of loans and receivables*

The bank's loan loss provisions are established to recognise incurred impairment losses either on specific loan assets or within a portfolio of loans and receivables.

Impairment losses for specific loan assets are assessed on an individual basis. Individual impairment losses are determined as the difference between the carrying value and the present value of estimated future cash flows, discounted at the loans' original effective interest rate.

Estimating the amount and timing of future recoveries involves significant judgement, and considers the level of arrears as well as the assessment of matters such as future economic conditions and the value of collateral, for which there may not be a readily accessible market.

Loan losses that have been incurred but have not been separately identified at the reporting date are determined on a portfolio basis, which takes into account past loss experience and defaults based on portfolio trends. Actual losses identified could differ significantly from the impairment provisions reported as a result of uncertainties arising from the economic environment.

(ii) *Fair value of financial instruments*

Where the fair values of the financial assets and liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable market data where possible, but where this is not feasible, a degree of judgment is required in establishing fair values.

(iii) *Taxation*

Judgment is required in determining the provision for income taxes due to the complexity of legislation. There are many transactions and calculations for which ultimate tax determination is uncertain during the ordinary course of business. The Bank recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

The Bank recognises the net future tax benefit that relates to deferred income tax assets to the extent that it is probable that the deductible temporary differences will reverse in the foreseeable future. Assessing the recoverability of deferred income tax assets requires the Bank to make significant estimates related to expectations of future taxable income. Estimates of future taxable income are based on forecast cash flows from operations and the application of existing tax laws in each jurisdiction. To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Bank to realise the net deferred tax assets recorded at the reporting date could be impacted.

4 FINANCIAL ASSETS AND LIABILITIES

Accounting classifications and fair values

31 March 2014:	Held for trading KShs'000	Available for sale KShs'000	Loans and receivables KShs'000	Others at amortised cost KShs'000	Fair value KShs'000
Financial assets			-		
Cash and balances with Central Bank of Kenya	-	-	-	4,481,682	4,481,682
Other assets – items in transit	-	-	-	943,054	943,054
Available for sale securities	-	29,254,359	-	-	29,254,359
Derivative financial instruments	67,522	-	-	-	67,522
Placements with other banks	-	-	-	3,396,930	3,396,930
Balances due from foreign branches	-	-	-	8,606,505	8,606,505
Loans and advances to customers	-	-	22,937,205	-	22,937,205
	67,522	29,254,359	22,937,205	17,428,171	69,687,257
Financial liabilities					
Deposits from banks	-	-	-	7,372,533	7,372,533
Deposits from customers	-	-	-	45,625,099	45,625,099
Derivative financial instruments	71,171	-	-	-	71,171
Other liabilities – items in transit and bills payable	-	-	-	1,554,730	1,554,730
	71,171	-	-	54,552,362	54,623,533
31 December 2013:					
Financial assets					
Cash and balances with Central Bank of Kenya	-	-	-	5,888,760	5,888,760
Other assets – items in transit	-	-	-	587,385	587,385
Available for sale securities	-	26,977,290	-	-	26,977,290
Derivative financial instruments	43,830	-	-	-	43,830
Placements with other banks	-	-	-	3,978,760	3,978,760
Balances due from foreign branches	-	-	-	6,395,749	6,395,749
Loans and advances to customers	-	-	24,211,853	-	24,211,853
	43,830	26,977,290	24,211,853	16,850,654	68,083,627
Financial liabilities					
Deposits from banks	-	-	-	8,904,920	8,904,920
Deposits from customers	-	-	-	43,813,617	43,813,617
Derivative financial instruments	-	-	-	-	135,662
Other liabilities – items in transit and bills payable	-	-	-	740,544	740,544
	135,662	-	-	53,459,081	53,594,743

4 FINANCIAL ASSETS AND LIABILITIES (Continued)

(a) Accounting classifications and fair values

The following sets out the branch's basis of establishing fair value of the financial instruments:

Derivative financial instruments

Derivative financial instruments are measured at fair value as set out in Note 15.

Cash and balances with Central Bank of Kenya

The fair value of cash and bank balances with the Central Bank of Kenya is their carrying amount.

Deposits and advances to banks

The fair value of floating rate placements and overnight deposits is their carrying amounts.

Loans and advances to customers

Loans and advances to customers are net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of future cash flows expected to be received, including assumptions relating to prepayment rates. Expected cash flows are discounted at current market rates to determine fair value. A substantial proportion of loans and advances reprice within 12 months and hence the carrying amount is a good proxy of the fair value.

Available for sale securities

Available for sale securities with observable market prices are fair valued using that information. The fair value is determined by discounting the securities using prevailing market rates.

Deposits from banks and customers

The estimated fair value of deposits with no stated maturity is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits without quoted market prices is based on discounting cash flows using the prevailing market.

A substantial proportion of deposits are within 6 months and hence the carrying amount is a good proxy of the fair value.

(b) Valuation hierarchy

The valuation hierarchy, and types of instruments classified into each level within that hierarchy, is set out below:

	Level 1	Level 2	Level 3
Fair value determined using:	Unadjusted quoted prices in an active market for identical assets and liabilities	Valuation models with directly or indirectly market observable inputs	Valuation models using significant non-market observable inputs

4 FINANCIAL ASSETS AND LIABILITIES (Continued)

The table below shows the classification of financial instruments held at fair value by the level in the fair value hierarchy as at 31 December 2013:

31 March 2014:	Level 1 KShs'000	Level 2 KShs'000	Level 3 KShs'000	Total KShs'000
Assets				
Available for sale securities	-	29,254,359	-	29,254,359
Derivative financial instruments	-	67,522	-	67,522
Total assets	-	29,321,881	-	29,321,881
Liabilities				
Derivative financial instruments	-	71,171	-	71,171
Total liabilities	-	71,171	-	71,171
31 December 2013:				
Available for sale securities	-	26,977,290	-	26,977,290
Derivative financial instruments	-	43,830	-	43,830
Total assets	-	25,074,012	-	25,074,012
Liabilities				
Derivative financial instruments	-	135,662	-	135,662
Total liabilities	-	135,662	-	135,662

5 ASSETS PLEDGED AS SECURITY

As at 31 December 2013 (2012 - Nil), there were no assets pledged by the bank to secure liabilities and there were no secured bank liabilities.

6 RELATED PARTY TRANSACTIONS

(a) Transactions with other Citibank branches and subsidiaries

In the normal course of business, transactions are entered into with other branches and subsidiaries of Citibank N.A, the parent company. During the year, the bank paid head office expenses amounting to KShs 17,037,481 (2013 - KShs 122,610,665) to other Citibank branches and subsidiaries. These transactions were carried out at arm's length.

The balances due from Citibank foreign branches are as disclosed under Note 17.

(b) Transaction with key management personnel

The Bank has entered into transactions with its key management personnel:

	2014 KShs '000	2013 KShs '000
Staff loans to key management personnel	<u>249,195</u>	<u>233,405</u>

Interest earned on these staff loans amounted to KShs 2,149,642 (2013 – KShs 11,670,239).

Interest rates charged on balances outstanding from employees are determined by the Senior Human Resource Committee and are granted at a discounted market interest rate. The mortgages and secured loans granted are secured over property and other assets of the respective borrowers.

No impairment losses have been recorded against balances outstanding during the period with key management personnel, and no specific allowance has been made for impairment losses on balances with key management personnel at the reporting date.

(c) Key management compensation

Compensation of the Bank’s key management personnel includes salaries, bonuses, non-cash benefits and contributions for retirement benefits under a defined contribution plan. Some bank officers also participate in the Parent’s share option programme.

	2013	2012
	KShs ‘000	KShs ‘000
Short term benefits	104,740	340,639
Other long term benefits	2,213	8,473
Share based payments	–	<u>23,992</u>
	<u>106,953</u>	<u>373,104</u>

7 PARENT COMPANY

The Bank is a branch of Citibank N.A, a national banking association formed under the laws of the United States of America. The ultimate holding company of the parent is Citigroup Inc.