2010
ANNUAL REPORT

ECB
Equatorial Commercial Bank

BANKING ON EXCELLENCE

OUR BRANCH NETWORK

NAIROBI BRANCHES

Equatorial Commercial Bank Centre, Nyerere Road
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Tel: +254(20) 4981000
Fax: +254(20) 2710700
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Avon Centre, Enterprise Road

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Fax: +254 (20) 554128
Email: customerservice@ecb.co.ke

Senator, Waiyaki Way
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MOMBASA BRANCHES

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Nyali Cinemax Complex, Kongowea Road
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KAKAMEGA BRANCH

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ELDORET BRANCH

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CONTENTS

BOARD MEMBERS AND COMMITTEES

DIRECTORS

Dan Ameyo, MBS	(Chairman - Appointed 31May 2010)
Peter Harris	(Managing Director - Appointed 31 May 2010)
M.H. Da Gama Rose	(Appointed on 31 May 2010)
Akif Hamid Butt	(Appointed on 31 May 2010)
Martin Ernest	(Appointed on 31 May 2010)
Jeffery Bamford	(Chairman - Resigned 31 May 2010)
Akbarali Kurji	(Ag. Managing Director - Resigned 31 May 2010)
Jones Nzomo	(Resigned 31 May 2010)
Muthoni Kuria (Mrs)	(Resigned 31 May 2010)
Richard Kemoli	(Resigned 31 May 2010)

SECRETARY

Fauzia B Shah (Mrs) (Appointed on 31 May 2010)
P.O. Box 55358
00200 Nairobi GPO

Reliable Associates (Resigned on 31 May 2010)
P.O. Box 39807
00623 Nairobi

AUDIT AND RISK COMMITTEE

Martin Ernest	Chairman
Akif Hamid Butt	
M.H. Da Gama Rose	

CREDIT COMMITTEE

Martin Ernest Chairman

CORPORATE INFORMATION

REGISTERED OFFICE

Equatorial Commercial Bank Centre (HQ)
Nyerere Road
PO Box 52467 - 00200
Nairobi

AUDITORS

KPMG Kenya
16th Floor, Lonrho House
PO Box 40612
00100 Nairobi GPO

CORRESPONDENT BANKS

- Habib American Bank Limited, New York
- Habibson Bank Limited, London
- Standard Chartered Bank, New York
- Standard Chartered Bank, London
- Standard Bank of South Africa, Johannesburg
- Standard Chartered Bank Kenya Limited, Nairobi
- Standard Chartered Bank Limited, Tokyo
- Commerzbank AG, Frankfurt
- ICICI Bank, Mumbai
- United Bank of Switzerland

ADVOCATES

- Aming'a, Opiyo, Masese & Co. Advocates
- Anjarwalla & Khanna Advocates
- C B Gor & Gor Advocates
- Gathaiya & Associates Advocates
- Gumbo & Associates
- Iseme Kamau & Maema Advocates
- J.Louis Onguto Advocates
- Joseph Munyithya & Co. Advocates
- Kwengu & Co. Advocates
- Macharia-Mwangi & Njeru Advocates
- Majanja Luseno & Co. Advocates
- Muri Mwaniki & Wamiti Advocates
- Muthaura Mugambi Ayugi & Njonjo Advocates
- Ndung'u Njoroge & Kwach Advocates
- Olel, Onyango Ingutia & Co. Advocates
- Shapley Barret & Company Advocates
- Shitsama & Co. Advocates
- Sichangi & Co Advocates
- Timamy & Co.
- Wambui Kyama & Co. Advocates

CHAIRMAN'S REPORT

The Board is pleased with the results achieved to date, and future growth is projected in line with corresponding improvements in the Bank's operating environment and the wider economy. Further gains are expected from the continued implementation of our Five Year Strategy.

ECONOMIC REVIEW

The overall 12 month inflation rate in December 2010 was 4.5%, an improvement from last year's 5.3% in December 2009.

The average yield rate for the 91 day treasury bills, a benchmark for the general trend of interest rates, rose to 2.276% in December 2010. The weighted average lending rate by commercial banks for loans and advances declined to 13.87% in December 2010 and savings rate was 1.45% in December 2010.

The Key event of this year was the merger of Equatorial Commercial Bank and Southern Credit Banking Corporation as of 31st May 2010.

BUSINESS AND PERFORMANCE REVIEW

Our balance sheet closed the year with total assets at Kshs. 10.4 billion compared to Kshs. 4.4 billion in December 2009 (the comparative figures are for SCBC and are prior to the merger), a 230% year on year increase. Gross loans and advances stood at Kshs. 5.3 billion compared to Kshs. 2.4 billion as at 31 December 2009. Customer deposits amounted to Kshs. 8.0 billion compared to Kshs. 4.3 billion at the end of 2009. Treasury bills & bonds increased to Kshs. 2.9 billion from Kshs. 692 million in 2009. We increased our investment in Equatorial Investment Bank by 20 million. These statistics make a strong statement for the Bank's intrinsic potential.

With increased customer deposits and a modestly favorable economic climate, the Bank recorded a loss after tax of Kshs 68 million at the end of the year compared to a loss of Kshs 108.7 million at the date of the merger. During the same period last year, the loss was Kshs 570 million. This means that post merger, the Bank made a profit of Kshs 40.6 million and this after deduction of integration costs of Kshs 85.9 million

The Bank grew its asset base to stand at Kshs 10.4 billion, fueled by a commensurate growth in customer deposits. Total operating income was Kshs 634.1 million, compared with Kshs. 297 million in 2009, with the growth mostly coming from interest income generated by the increased loan portfolio. The Bank's Non interest income was Kshs 338.1 million, mainly driven by commissions and fees from transactions. Operating expenses were 592.16 million and exceptional integration costs of 142.8 million.

CHAIRMAN'S REPORT cont...

CONCLUDING REMARKS

I wish to take this opportunity to express my gratitude to all employees of ECB for their efforts during the transition period and without whose commitment the merger would not have been completed so successfully. I also express my appreciation to our customers who kept faith with us.

The organizational transformation project, with the objective of achieving an even more focused and results oriented institution, continued during the year. This is an integral part of an ongoing re-alignment of our strategy to position the Bank for success in this increasingly competitive environment.

In conclusion, I wish to express my gratitude to my fellow directors for their guidance and support throughout the year. My sincere thanks to Management and Staff for their invaluable contribution towards the progress the Bank has made during the year, their hard work and professionalism. I also take this opportunity to convey my appreciation to all our customers for giving ECB the opportunity to remain their financial institution of choice.

Dan Ameyo, MBS
CHAIRMAN

CORPORATE GOVERNANCE

Equatorial Commercial Bank Limited is committed to implementing ongoing initiatives to improve corporate governance for the benefit of all stakeholders.

The Bank's Board of Directors is focused on achieving compliance with qualitative aspects of good governance while ensuring that implementation meets the business needs.

The Board has also established Board Committees with delegated authority from the Board to assist it in providing Board oversight on management functions and in fulfilling the stated objectives of the Board. The Committees' roles and responsibilities are set out in Terms of Reference and agreed mandates, which are reviewed periodically to ensure they remain relevant.

CODES AND REGULATIONS

As a licensed Commercial Bank, the Bank operates in a highly regulated industry and is committed to complying with legislation, regulations and codes of best practice and seeks to maintain the highest standards of governance, including transparency and accountability.

The Bank complies with applicable legislation, regulations, standards and codes, with the Board continuously monitoring regulatory compliance to guidelines issued by the Central Bank of Kenya and other regulatory bodies. The Board also monitors overall adherence to best practices in the Bank.

BOARD OF DIRECTORS

The Bank is governed by the Board of Directors, which has ultimate responsibility for the management and strategic guidance of the company and assumes the primary responsibility for the sustainability of the company's business.

BOARD COMPOSITION

There are five directors on the Board of whom one is executive and four are non-executive. The Board is therefore compliant with guidelines issued by the Regulator on composition of the Board.

The members of the Board have the right mix of skills, expertise, competencies and experience to effectively guide the Bank and ensure that the objective of shareholder value maximization is achieved.

The Board profile is regularly reviewed to ensure that the Board composition remains appropriate given the dynamics of the banking industry.

STRATEGY

The Board is fully aware of its obligations to shareholders and other stakeholders for forging the strategic direction that the Bank will follow, and in so doing meets with the Executive Committee to consider and approve the Bank's strategy for the years ahead. Currently, the Bank is embarking on fulfillment of all aspects of its Board approved 5 year Strategic Plan approved in 2010. Regular reports to the Board on progress are tabled at Board meetings for review, noting any deliberations by members of the Board.

The performance against financial objectives is monitored by the Board through management's monthly, quarterly and annual reporting.

DELEGATION AND EFFECTIVE CONTROL

The ultimate responsibility of the Bank's operations rests with the Board. The Board retains effective control through a well developed governance structure of Board committees. These committees provide in depth focus on specific areas of Board responsibility.

Authority has been delegated to the Managing Director to manage the business together with his management committees comprising of senior managers and unit heads.

Further delegations are managed through a defined process.

The Managing Director is tasked with the implementation of Board decisions and there is a clear flow of information between management and the Board, which facilitates both the qualitative and quantitative evaluation of the Bank's performance.

EVALUATION OF BOARD EFFECTIVENESS

Annually, the ECB Board carries out a self review of its capacity, functionality and effectiveness. The evaluation measures the performance of the Board against its key duties and responsibilities.

BOARD MEETINGS

The Board meets at a minimum of once every quarter with additional meetings scheduled to discuss strategy. Additional meetings are held whenever deemed necessary. Directors are provided with comprehensive documentation at least seven days prior to each of the scheduled meetings.

BOARD COMMITTEES

The Board has established the Board Audit and Risk Committee and the Board Credit Committee to assist it in discharging its responsibilities.

The role of the Board Audit and Risk Committee is to review the Bank's financial position and make recommendations to the Board on all financial matters. This includes assessing the integrity and effectiveness of accounting, financial, compliance and other control systems. This committee also provides Board oversight of the Bank's risk management framework in all functions of the Bank.

The role of the Board Credit Committee is to review the Bank's Credit Policy and ensure adherence to the same by Management. This Committee also reviews facilities that are beyond the discretionary limits of the Management Credit Risk Committee and ensures that measures are in place to mitigate, measure, monitor and manage credit risk at all times.

MANAGEMENT COMMITTEES

The following management committees are in place to ensure that the Bank carries out its obligations efficiently and effectively:

- Asset and Liability Committee;
- Risk Management Committee;
- Product and IT Committee; and
- Management Credit Risk Committee.

FEES

Non-executive directors receive fixed fees for service on the Board. The Board reviews the non-executive directors' fees annually and makes appropriate recommendations to the Shareholders at the Annual General Meeting for approval.

COMPANY SECRETARY

The Company Secretary provides the Board with guidance on its responsibilities and keeps directors up-to-date with changes to relevant legislation as well as governance best practices.
All directors have access to the services of the Company Secretary.

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2010

The Directors have pleasure in submitting their report together with the audited financial statements for the year ended 31 December 2010.

1. ACTIVITIES

The company is engaged in the business of commercial banking and provision of related services and is licensed under the Banking Act.

The company has a 20% investment in Equatorial Investment Bank Limited and 23.86% (2009 – 24.42%) in Fidelity Shield Insurance Company Limited which have been accounted for as associate companies in the consolidated financial statements.

2. SUMMARY OF MERGER TRANSACTION

On 31 May 2010, the merger of Equatorial Commercial Bank Limited (ECB) with Southern Credit Banking Corporation Limited (SCBC) was concluded.

ECB was a privately owned Bank operating a commercial banking business with an associated company engaged in investment banking.

SCBC is a public limited company, operating a commercial banking business, and in addition running the Senator credit card business. SCBC has an associated company engaged in general insurance business.

The merger transaction was structured in four interlinked phases:

(i) In order to raise additional capital of Kshs 264 million to meet the capital adequacy requirements of the merged Bank, ECB implemented a rights issue to increase its authorized and issued share capital by an additional Two Million Six Hundred and Forty One Thousand Seven Hundred and Ten (2,641,710) ordinary shares which were issued to the existing shareholders pro rata to their shareholding at par value;

(ii) ECB acquired new shares in SCBC in exchange for its own shares, thereby making SCBC a subsidiary of ECB. By way of a Share Acquisition and Swap Agreement, ECB acquired Seventy Seven Million, Five Hundred and Eleven Thousand, One Hundred and Thirty (77,511,130) new ordinary shares in SCBC representing 83.96% of the authorized and issued share capital of SCBC as consideration for acquiring One Million and Ninety Five Thousand Four Hundred and Twenty Eight (1,095,428) new ordinary shares representing 11.25% of the issued share capital of ECB.

(iii) ECB and SCBC then executed an Asset and Portfolio (Business) Transfer Agreement for the merger of ECBs banking business, assets and liabilities in to SCBC who paid a fair consideration for the merger of the business by the issue of 208,323,400 new shares equal in value to the assets and liabilities being merged of Kshs 1,041,616,000.

(iv) The merged Bank adopted the name Equatorial Commercial Bank Limited and former ECB changed its name to Equatorial Holding Limited and became the holding company of the merged Bank.

All the necessary regulatory approvals were received and all conditions precedent met by 31 May 2010.

The carrying values of the assets and liabilities of ECB at 31 May 2010 were equivalent to their fair values.

The consideration was entirely satisfied by the issue of shares and there was no cash outflow.

2. SUMMARY OF MERGER TRANSACTION (CONTINUED)

MERGER ACCOUNTS

The table below highlights the balance sheet movements as a result of the merger of ECB into SCBC:

Merger at 31 May 2010	SCBC 31.05.2010 KShs'000	Merger of ECB 31.05.2010 KShs'000	Merged Bank 31.05.2010 KShs'000
Assets			
Cash and balances with Central Bank of Kenya	153,982	48,736	**202,718**
Cash reserve ratio	163,300	159,853	**323,153**
Government securities	544,535	1,707,359	**2,251,894**
Local bank deposits	661,894	544,780	**1,206,674**
Foreign bank deposits	33,572	511,303	**544,875**
Corporate bond	243,158	93,200	**336,358**
Loans and advances (net of provisions)	1,714,063	2,513,401	**4,227,464**
Investments in associate companies	104,056	30,000	**134,056**
Property and equipment	254,305	35,703	**290,008**
Intangible assets	7,161	10,158	**17,319**
Investment property	163,620	-	**163,620**
Prepaid operating leases	12,788	-	**12,788**
Deferred tax asset	373,012	27,149	**400,161**
Other assets	73,877	55,767	**129,644**
Total assets	**4,503,323**	**5,737,409**	**10,240,732**
Liabilities			
Balances due to Central Bank of Kenya	-	159,930	**159,930**
Deposits from Banking Institutions	894,466	553,115	**1,447,581**
Customer deposits	3,595,303	3,916,056	**7,511,359**
Tax payable	-	17,538	**17,538**
Other liabilities	127,195	49,154	**176,349**
Total liabilities	**4,616,964**	**4,695,793**	**9,312,757**
Net assets	**(113,641)**	**1,041,616**	**927,975**
Share capital	461,622	1,041,616	**1,503,238**
Retained earnings (deficit)	(592,324)	(41,100)	**(633,424)**
Current year loss	(108,704)	-	**(108,704)**
Revaluation reserve	47,412	-	**47,412**
Statutory reserve	78,353	41,100	**119,453**
Shareholders' funds	**(113,641)**	**1,041,616**	**927,975**

3. CHANGE OF NAME

The Bank changed its name from Southern Credit Banking Corporation Limited to Equatorial Commercial bank Limited on 31 May 2010.

4. RESULTS

The results for the year are set out on page 16.

5. DIVIDEND

The Directors do not propose a dividend for the year (2009 - Nil).

6. DIRECTORS

The Directors who served during the year are set out on page 1. The following table shows the rate of attendance of Board meetings by the current Directors:

Director's name	Nationality	Executive/ Non-Executive	Profession	Attendance for Board meetings
M.H. Da Gama Rose	Kenyan	Non Executive	Advocate	100%
Akif Hamid Butt	Kenyan	Non Executive	Chartered Accountant	100%
Peter Harris	British	Executive	Banker	100%
Martin Ernest	British	Non Executive	Chartered Accountant	100%
Dan Ameyo	Kenyan	Non Executive	Advocate	100%

7. AUDITORS

The auditors, KPMG Kenya, were appointed during the year and have indicated their willingness to continue in office in accordance with Section 159(2) of the Kenyan Companies Act (Cap. 486) and subject to Section 24(1) of the Banking Act (Cap. 488).

8. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved at a meeting of the Directors held on 18 March 2011.

BY ORDER OF THE BOARD

Fauzia B. Shah (Mrs)
Company Secretary
Date: 18 March 2011

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for the preparation and presentation of the Group financial statements of Equatorial Commercial Bank Limited (formerly Southern Credit Banking Corporation Limited) set out on pages 14 to 59 which comprise the statement of financial position of the group and the company at 31 December 2010, the group's statement of comprehensive income, the group and company statement of changes in equity and group statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

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

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

The Directors accept responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act. The Directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the group and the company and of the group operating results.

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

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

APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements, as indicated above, were approved by the Board of Directors on 18 March 2011 and were signed on its behalf by:

Director

Director

Director

Secretary

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

We have audited the Group financial statements of Equatorial Commercial Bank Limited (formerly Southern Credit Banking Corporation Limited) set out on pages 16 to 62 which comprise the statement of financial position of the Group and the company at 31 December 2010, and the Group's statement of comprehensive income, the group and company statement of changes in equity and group cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

As stated on page 9, the directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

OPINION

In our opinion, the financial statements give a true and fair view of the financial position of the Group and the company at 31 December 2010, and the Group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the Kenyan Companies Act.

REPORT ON OTHER LEGAL REQUIREMENTS

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

(i) We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purpose of our audit;

(ii) In our opinion, proper books of account have been kept by the company, so far as appears from our examination of those books; and

(iii) The statement of financial position of the company is in agreement with the books of account.

Date: 18 March 2011

KPMG Kenya

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2010

	Notes	2010 KShs'000	2009 KShs'000
Interest income	7	687,116	440,617
Interest expense	8	(391,193)	(309,134)
Net interest income		**295,923**	**131,483**
Fee and commission income		105,938	73,539
Foreign exchange trading income		52,028	314
Changes in fair valuation of investment property		-	77,444
Other operating income	9	180,197	14,142
Operating income		**634,086**	**296,922**
Impairment losses on financial assets	19 (b)	(75,432)	(593,031)
Operating expenses	10	(734,969)	(459,398)
Share of profit of associate companies	23	38,720	25,955
Loss before taxation	12	(137,595)	(729,552)
Income tax credit	13	69,531	159,593
Loss for the year after taxation		**(68,064)**	**(569,959)**
Other Comprehensive Income			
Surplus on revaluation of property		-	67,732
Deferred tax on revaluation surplus		20,320	(20,320)
Transfer to statutory credit risk reserve		(18,042)	-
		2,278	47,412
Total Comprehensive Loss		**(65,786)**	**(522,547)**
Basic and diluted loss per share– KShs	**14**	**(0.32)**	**(6.17)**
Dividend per share – KShs	**15**	**-**	**-**

The notes on pages 22 to 62 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2010

	Note	2010 KShs'000	2009 KShs'000
ASSETS			
Cash and balances with Central Bank	16	656,778	306,044
Investments in government securities	17	2,996,145	692,051
Investments in corporate bonds	17	335,545	235,400
Placements with other Banks	18	329,841	408,111
Loans and advances to customers	19(a)	4,851,414	1,953,299
Property and equipment	20	114,609	191,773
Intangible assets	21	14,894	7,374
Prepaid operating lease rentals	22	-	12,788
Investment in associate companies	23	172,776	104,056
Deferred tax asset	24	430,339	313,339
Investment property	25	-	163,749
Balance due from Parent Company	26	403,525	-
Other assets	27	157,613	103,391
TOTAL ASSETS		**10,463,479**	**4,491,375**
LIABILITIES AND SHAREHOLDERS' EQUITY			
LIABILITIES			
Deposits from Banking Institutions		1,295,754	15,000
Customers deposits	28	8,036,584	4,307,696
Other liabilities	29	160,249	173,617
TOTAL LIABILITIES		**9,492,587**	**4,496,313**
SHAREHOLDERS' EQUITY			
Share capital	30(a)	1,503,238	461,622
Retained earnings (deficit)		(628,998)	(592,324)
Revaluation reserve		-	47,412
Statutory credit risk reserve	30(b)	96,652	78,352
TOTAL EQUITY ATTRIBUTABLE TO SHAREHOLDERS		**970,892**	**(4,938)**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**10,463,479**	**4,491,375**

The financial statements on pages 16 to 62 were approved by the Board of Directors on 18 March 2011 and were signed on its behalf by:

Director ______________________ Director ______________________

Director ______________________ Secretary ______________________

The notes on pages 22 to 62 form an integral part of these financial statements.

COMPANY STATEMENT OF FINANCIAL POSTION AS AT 31 DECEMBER 2010

	Note	2010 KShs'000	2009 KShs'000
ASSETS			
Cash and balances with Central Bank	16	656,778	306,044
Investments in government securities	17	2,996,145	692,051
Investments in corporate bonds	17	335,545	235,400
Placements with other Banks	18	329,841	408,111
Loans and advances to customers	19(a)	4,851,414	1,953,299
Property and equipment	20	114,609	191,773
Intangible assets	21	14,894	7,374
Prepaid operating lease rentals	22	-	12,788
Investment in associate companies	23	108,101	78,101
Deferred tax asset	24	430,339	313,339
Investment property	25	-	163,749
Balance due from Parent Company	26	403,525	-
Other assets	27	157,613	103,391
TOTAL ASSETS		**10,398,804**	**4,465,420**
LIABILITIES AND SHAREHOLDERS' EQUITY			
LIABILITIES			
Deposits from Banking Institutions		1,295,754	15,000
Customers deposits	28	8,036,584	4,307,696
Other liabilities	29	160,249	173,617
TOTAL LIABILITIES		**9,492,587**	**4,496,313**
SHAREHOLDERS' EQUITY			
Share capital	30(a)	1,503,238	461,622
Retained earnings (deficit)		(693,673)	(618,279)
Revaluation reserve		-	47,412
Statutory credit risk reserve	30(b)	96,652	78,352
TOTAL EQUITY ATTRIBUTABLE TO SHAREHOLDERS		**906,217**	**(30,893)**
TOTAL LIABILITIES AND SHAREHOLDERS'EQUITY		**10,398,804**	**4,465,420**

Director ______________ Director ______________

Director ______________ Secretary ______________

The notes on pages 22 to 62 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2010

	Share Capital	Retained earnings	Revaluation reserve	Statutory credit risk reserve	Total
2009:	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**	**KShs'000**
Balance at 1 January 2009	461,622	(9,721)	-	65,708	517,609
Comprehensive Loss for the year					
Loss for the year	-	(569,959)	-	-	(569,959)
Other comprehensive income					
Revaluation Surplus on property	-	-	67,732	-	67,732
Appropriation to statutory credit risk reserve	-	(12,644)	-	12,644	-
Deferred tax on revaluation surplus	-	-	(20,320)	-	(20,320)
Total other comprehensive income	-	(12,644)	47,412	12,644	47,412
Total comprehensive income for the year	-	(582,603)	47,412	12,644	522,547
Balance at 31 December 2009	**461,622**	**(592,324)**	**47,412**	**78,352**	**(4,938)**
2010:					
Balance at 1 January 2010	461,622	(592,324)	47,412	78,352	(4,938)
Comprehensive Loss for the year					
Loss for the year	-	(68,064)	-	-	(68,064)
Other comprehensive income					
Revaluation Surplus on property	-	67,732	(67,732)	-	-
Acquisition through business combination	-	(41,100)	-	41,100	-
Appropriation to statutory credit risk reserve	-	4,758	-	(22,800)	(18,042)
Deferred tax on revaluation surplus	-	-	20,320	-	20,320
Total other comprehensive income	-	31,390	(47,412)	18,300	2,278
Total comprehensive income for the year	**-**	**(36,674)**	**(47,412)**	**18,300**	**(65,786)**
Transaction with owners recorded Directly in equity					
Issue of ordinary shares on merger	1,041,616	-	-	-	1,041,616
At 31 December 2010	**1,503,238**	**(628,998)**	**-**	**96,652**	**970,892**

COMPANY STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2010

	Share capital KShs'000	Retained earnings KShs'000	Revaluation reserve KShs'000	Statutory credit risk reserve KShs'000	Total KShs'000
Balance at 1 January 2009	461,622	(9,721)	-	65,708	517,609
Comprehensive Loss for the year					
Loss for the year	-	(595,914)	-	-	(595,914)
Other comprehensive income					
Revaluation Surplus on property	-	-	67,732	-	67,732
Appropriation to statutory credit risk reserve	-	(12,644)	-	12,644	-
Deferred tax on revaluation surplus	-	-	(20,320)	-	(20,320)
Total other comprehensive income	-	(12,644)	47,412	12,644	47,412
Total comprehensive income for the year	**-**	**(608,558)**	**47,412**	**12,644**	**(548,502)**
Balance at 31 December 2009	**461,622**	**(618,279)**	**47,412**	**78,352**	**(30,893)**
2010:					
Balance at 1 January 2010	461,622	(618,279)	47,412	78,352	(30,893)
Comprehensive Loss for the year					
Loss for the year	-	(106,784)	-	-	(106,784)
Other comprehensive income					
Revaluation Surplus on property	-	67,732	(67,732)	-	-
Acquisition through business combination	-	(41,100)	-	41,100	-
Appropriation to statutory credit risk reserve	-	4,758	-	(22,800)	(18,042)
Deferred tax on revaluation surplus	-	-	20,320	-	20,320
Total other comprehensive income	-	31,390	(47,412)	18,300	2,278
Total comprehensive income for the year	**-**	**(75,394)**	**(47,412)**	**18,300**	**(104,506)**
Transaction with owners recorded Directly in equity					
Issue of ordinary shares on merger	1,041,616	-	-	-	1,041,616
At 31 December 2010	**1,503,238**	**(693,673)**	**-**	**96,652**	**906,217**

The notes on pages 22 to 62 form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CASHFLOW
FOR THE YEAR ENDED 31 DECEMBER 2010

	Note	2010 KShs'000	2009 KShs'000
Net cash outflow from operating activities	32(a)	**(1,509,422)**	**328,760**
Cash flows from investing activities			
Purchase of other financial assets		-	(235,400)
Purchase of property and equipment		(66,972)	(40,945)
Purchase of investment property		-	(86,305)
Addition of prepaid operating lease rentals		-	(12,788)
Purchase of intangible assets		(1,527)	(7,986)
Proceeds from disposal of property and equipment		3,664	975
Proceeds from disposal of investment property		-	64,471
Net cash used in investing activities		**(64,835)**	**(317,978)**
Net cash acquired	31	391,774	-
(Decrease)/increase in cash and cash equivalents	32(b)	**(1,182,483)**	**10,782**

The notes on pages 22 to 62 form an integral part of these financial statements

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010

1. REPORTING ENTITY

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

Equatorial Commercial Bank Centre (HQ)
Nyerere Road
P O Box 52467 - 00200
Nairobi

2. BASIS OF PREPARATION

(a) Statement of compliance

The financial statements are prepared in accordance with and comply with International Financial Reporting Standards. The financial statements are prepared under the historical cost basis as modified by the revaluation of financial instruments, classified as instruments available for sale, held for trading, instruments held at fair value through statement of comprehensive income and derivative instruments.

(b) Use of estimates and judgments

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

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

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

(c) Functional and presentation currency

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

Items included in the financial statements are measured using the currency of primary economic environment in which the entity operates i.e. Kenya shillings.

3. SIGNIFICANT ACCOUNTING POLICIES

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

(a) Basis of consolidation

The consolidated financial statements include the company and its associates made up to the end of the financial year. The associates are set out on Note 23.

(b) Revenue recognition

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

(i) Net interest income

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

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(ii) Fees and commission income

Fees and commission income is recognized on an accrual basis when the service is provided.

(iii) Foreign exchange trading income

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

(c) Recognition and measurement of financial instruments

The Bank classifies its financial assets into four categories described below. Management determines the appropriate classification of its financial instruments at the time of purchase and re-evaluates its portfolio on a regular basis to ensure that all financial assets are appropriately classified.

(i) Financial assets at fair value through profit or loss

Financial assets in this category held for trading are those that the Group principally holds for the purpose of short-term profit taking and/or those designated at fair value through profit or loss at inception. These are recognised on the date the Group commits to acquire the instruments.

Trading instruments are initially recognised at cost, including transaction costs. Subsequent to initial recognition, trading instruments are stated at fair value based on quoted bid prices. Where the fair value cannot be reliably measured, the assets are stated at cost less impairment losses. Changes in fair value are recognised in profit or loss.

(ii) Loans and receivables

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

They arise when the Bank provides money directly to borrowers, other than those created with the intention of short-term profit taking. They are recognised at the date money is disbursed to the borrower or when they are transferred to the Bank from a third party.

Subsequent to initial recognition, these are carried at amortised cost, which is the present value of the expected future cash flows, discounted at the instrument's original effective interest rate. Loan origination fees together with related direct costs are treated as part of the cost of the transaction.

Amortised cost is calculated using the effective interest rate method. The amortisation and accretion of premiums and discounts is included in interest income.

(iii) Held-to-maturity

These are 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. The sale of a significant amount of held-to-maturity assets would taint the entire category leading to reclassification as available-for-sale.

Subsequent to initial recognition, these are carried at amortised cost, which is the present value of the expected future cash flows, discounted at the instrument's original effective interest rate.

Amortised cost is calculated using the effective interest rate method. The amortisation and accretion of premiums and discounts is included in interest income.

(iv) Available-for-sale

Other financial assets held by the Bank are classified as available-for-sale and are initially recognised at cost, including transaction costs. Subsequent to initial recognition, available for sale financial assets are stated at fair value based on quoted bid prices. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity in the fair value reserve, net of deferred tax. When these investments are derecognised, the cumulative gain or loss previously directly recognised in equity is recognised in profit or loss.

Derecognition

A financial asset is derecognised when the Bank loses control over the contractual rights that comprise that asset. This occurs when the rights are realised, expire or are surrendered. A financial liability is derecognised when it is extinguished.

Available-for-sale assets and assets held for trading that are sold are derecognised and corresponding receivables from the buyer for the payment are recognised as of the date the Bank commits to sell the assets. The Bank uses the specific identification method to determine the gain or loss on derecognition.

Held-to-maturity instruments and loans and receivables are derecognised on the day they are repaid in full or when they are transferred by the Bank to a third party.

(d) 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.

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

Objective evidence that financial assets 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.

(d) Identification and measurement of impairment of financial assets (continued)

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 the 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 out of 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 the profit or loss.

However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised directly in equity. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

(e) Impairment for non-financial assets

The carrying amounts of the Bank's non-financial assets, other than deferred tax asset, 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.

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 largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro-rata basis.

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.

(f) Translation of foreign currencies

Transactions in foreign currencies during the year are converted into Kenya Shillings at the exchange rate ruling at the date of the transaction. Foreign currency monetary assets and liabilities are translated at the exchange rate ruling at the reporting date. Resulting exchange differences are recognised in profit or loss for the year.

(g) Property and equipment

(i) Recognition and measurement

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

(ii) Depreciation

Depreciation is charged on a straight-line basis over the estimated useful lives of the assets. The rates of depreciation used are based on the following estimated useful lives:

• Motor vehicles	4 years
• Computer equipment	4 years
• Office equipment	5 years
• Fixtures and fittings	4 to 10 years

Depreciation methods, useful lives and residual values are reassessed and adjusted, if appropriate, at each reporting date.

(iii) Subsequent costs

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

(iv) Disposal of property and equipment

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are recognised in the profit or loss in the year in which they arise.

(h) Intangible assets

The cost 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, for a period not exceeding three years. Costs associated with maintaining software are recognised as an expense as incurred.

(i) 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 charged to profit or loss on a straight line basis over the period of the lease.

(j) Income tax expense

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

Deferred tax is provided using the statement of financial position liability method on all 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 on the basis of the tax rates currently enacted.

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 tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(k) Employee benefits

(i) Defined contribution plan

The majority of the Bank's employees are eligible for retirement benefits under a defined contribution plan.

Contributions to the defined contribution plan are charged to the profit or loss as incurred. Any difference between the charge to the profit or loss and the contributions payable is recorded in the statement of financial position under other receivables or other payables.

The company also contributes to a statutory defined contribution pension scheme, the National Social Security Fund (NSSF). Contributions are determined by local statute and are currently limited at KShs 200 per employee per month.

(ii) Leave accrual

The monetary value of the unutilised leave by staff as at year end is carried in the accruals as a payable and the movement in the year is debited /credited to the profit or loss.

(iii) Termination benefits

Termination benefits are recognised as an expense when the Group is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to

terminate employment before the normal retirement date. Termination benefits for voluntary redundancies are recognised if the Group has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

(l) Cash and cash equivalents

For the purpose of presentation of the cash flows in the financial statements the cash and cash equivalents include cash and balances with Central Bank of Kenya available to finance the Bank's day-to-day operations, net balances from Banking institutions and treasury bills and bonds which mature within 90 days or less from the date of acquisition.

(m) Dividends

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

(n) Related parties

In the normal course of business, transactions have been entered into with certain related parties. These transactions are at arm's length.

(o) Provisions

Provisions are recognised when the company has a present legal or constructive obligation as a result of past events and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made.

(p) Offsetting of financial assets and liabilities

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

(q) Contingent liabilities

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

(r) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss for the year attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss for the year attributable to ordinary shareholders and the weighted average number of shares outstanding to the effects of all dilutive potential ordinary shares, if any.

(s) New standards and interpretations not yet adopted

A number of amendments to standards and interpretations are effective for the year ended 31 December 2010:

- IAS 24 *'Related party disclosures'* amends the definition of a related party and modifies certain related party disclosure requirements for government related entities. The amendment to IAS 24 will become mandatory for the Group's 2011 financial statements and are expected to have an impact on the presentation of related party information in the Group's financial statements.

- IFRS 9 *'Financial Instruments'* retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortised costs and fair value. The basis for classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply.

  IFRS 9 will become mandatory for the Group's 2014 financial statements and is not expected to have a significant effect on the financial statements.

4. FINANCIAL RISK MANAGEMENT

(a) Introduction and overview

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

- Credit risk
- Liquidity risk
- Market risks
- Operational risks

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

Risk management framework

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

The Bank's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered.

The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

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

(b) Credit risk

The Bank's credit exposure at the reporting date from financial instruments held or issued for trading purposes is represented by the fair value of instruments with a positive fair value at that date, as recorded on the statement of financial position.

The risk that counter-parties to trading instruments might default on their obligations is monitored on an ongoing basis. In monitoring credit risk exposure, consideration is given to trading instruments with a positive fair value and to the volatility of the fair value of trading instruments.

To manage the level of credit risk, the Bank deals with counter-parties of good credit standing, enters into master netting agreements whenever possible, and when appropriate, obtains collateral. An assessment of the extent to which fair values of collaterals cover existing credit risk exposures on loans and advances to customers is highlighted in the later part of this section.

The Bank also monitors concentrations of credit risk that arise by industry and type of customer in relation to the Bank loans and advances to customers by carrying a balanced portfolio. The Bank has no significant exposure to any individual customer or counter-party.

The group exposure to credit risk is analysed as follows:

	2010 KShs'000	2009 KShs'000
(i) Loans and advances to customers		
Individually impaired		
Impaired (substandard)	403,590	166,480
Impaired (doubtful)	676,954	776,270
Impaired (loss)	117,564	50,840
Gross amount	1,198,108	993,590
Allowance for impairment	(472,630)	(472,832)
Carrying amount	**725,478**	**520,758**
Collectively impaired		
Neither Past due nor impaired	3,803,113	1,071,150
Past due and not impaired	336,068	361,391
Gross amount	4,139,181	1,432,541
Portfolio impairment provision	(13,245)	-
Carrying amount	**4,125,936**	**1,432,541**
Total Carrying amount	**4,851,414**	**1,953,299**
(ii) Other financial assets		
Neither past due nor impaired		
Investment in Government securities	2,996,145	692,051
Corporate bonds	335,545	235,400
Placements with other Banks	**329,841**	**408,111**

Impaired loans and securities
Impaired loans and securities are loans and securities for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan / securities agreement(s). These loans are graded substandard, doubtful and loss in the Group's internal credit risk grading system.

Past due but not impaired loans
Loans and securities where contractual interest or principal payments are past due but the Group believes that impairment is not appropriate on the basis of the level of security / collateral available and / or the stage of collection of amounts owed to the Group.

Loans with renegotiated terms
Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Group has made concessions that it would not otherwise consider. Once the loan is restructured it remains in this category independent of satisfactory performance after restructuring.

Allowances for impairment
The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

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

For smaller balance standardised loans, charge off decisions generally are based on a product specific past due status.

Set out below is an analysis of the gross and net of allowances for impairment amounts of individually impaired assets by risk grade.

Loans and advances to customers	Gross KShs'000	Net KShs'000
31 December 2010:		
Impaired (substandard)	403,590	300,365
Impaired (doubtful)	676,954	413,459
Impaired (loss)	117,564	11,654
	1,198,108	**725,478**
31 December 2009:		
Impaired (substandard)	166,480	96,221
Impaired (doubtful)	776,270	411,026
Impaired (loss)	50,840	13,511
	993,590	**520,758**

The Group holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to Banks, except when securities are held as part of reverse repurchase and securities borrowing activity. Collateral usually is not held against investment securities, and no such collateral was held at 31 December 2010 or 2009.

An estimate of the fair value of collateral and other security enhancements held against financial assets is shown below:

Loans and advances to customers	**2010 KShs'000**	**2009 KShs'000**
Against individually impaired		
Property	949,912	402,541
Other	75,538	-
Against collectively impaired		
Property	3,728,664	179,847
Debt securities	375,306	-
Equities	142,254	-
Other	1,017,582	-
Against past due but not impaired		
Property	96,717	179,847
Debt securities	10,300	-
Other	72,000	-
Against neither past due nor impaired		
Property	3,631,947	-
Debt securities	365,006	-
Equities	142,254	-
Other	945,582	-

The Group monitors concentrations of credit risk by sector. An analysis of concentrations of credit risk at the reporting date is shown below:

Gross Loans and advances to customers

	2010 KShs'000	2009 KShs'000
Carrying amount		
Building and construction	422,734	346,393
Wholesale and retail trade, restaurants and hotels	2,772,162	1,213,800
Finance and insurance	8,508	152
Manufacturing	734,845	87,656
Social, community, personal services	259,320	284,955
Agriculture	552,229	103,266
Others	587,489	389,909
	5,337,287	**2,426,131**

Settlement risk

The Group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed.

For certain types of transactions the Group mitigates this risk by conducting settlements through a settlement/clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval/limit monitoring process described earlier. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals from Group Risk.

(c) Liquidity risk

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 time frame.

The Bank has access to a diverse funding base. Funds are raised mainly from deposits and share capital. This enhances funding flexibility, limits dependence on any one source of funds and generally lowers the cost of funds. The Bank strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with a range of maturities. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall Bank strategy.

In addition the Bank holds a portfolio of liquid assets as part of its liquidity risk management strategy.

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

Management of liquidity risk

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

Central Treasury receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business.

Central Treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to Banks and other inter-Bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions. All liquidity policies and procedures are subject to review and approval by ALCO. Daily reports cover the liquidity position of both the Group and operating subsidiaries and foreign branches. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO.

Exposure to liquidity risk

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets are considered as including cash and cash equivalents and investment grade debt securities for which there is an active and liquid market less any deposits from Banks, debt securities issued, other borrowings and commitments maturing within the next month.

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

	2010	2009
At 31 December	33.7%	40.0%
Average for the period	39.1%	36.8%
Maximum for the period	57.7%	40.0%
Minimum for the period	23.0%	30.6%

The table below analyses financial liabilities of the Bank into relevant maturity groupings based on the remaining period at 31 December 2010 to the contractual maturity date.

	On demand KShs'000	Due within 3 months KShs'000	Due between 3-12 months KShs'000	Due between 1-5 years KShs'000	Total KShs'000
31 December 2010:					
LIABILITIES					
Deposits from banking institutions	-	1,295,754	-	-	**1,295,754**
Customer deposits	2,329,385	2,439,211	3,048,629	219,359	**8,036,584**
Other liabilities	160,249	-	-	-	**160,249**
TOTAL LIABILITIES	**2,489,634**	**3,734,965**	**3,048,629**	**219,359**	**9,492,587**
31 December 2009:					
LIABILITIES					
Deposits from banking institutions	-	15,000	-	-	**15,000**
Customer deposits	1,361,467	2,240,818	653,664	51,747	**4,307,696**
Other liabilities	173,617	-	-	-	**173,617**
TOTAL LIABILITIES	**1,535,084**	**2,255,818**	**653,664**	**51,747**	**4,496,313**

(d) Market risk

Interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest earning assets and interest bearing liabilities mature or reprice at different times or in differing amounts. Risk management activities are aimed at optimizing net interest income, given market interest rates levels consistent with the company's business strategies.
The company does not have any significant interest rate risk exposures.

This table shows the extent to which the group's interest rate exposures on assets and liabilities are matched. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and maturity date:

31 December 2010:	Effective interest rate %	3 months or less KShs'000	Over 3 months KShs'000	Non-interest bearing KShs'000	Total KShs'000
ASSETS					
Cash and balances with Central Bank of Kenya				656,778	**656,778**
Investments in Government securities	6.33%	268,900	2,727,245		**2,996,145**
Placements with other banks	2.74%	329,841	-		**329,841**
Investment in corporate bonds	12.50%	-	335,545		**335,545**
Loans and advances to customers	11.41%	3,233,456	1,617,958		**4,851,414**
Property and equipment	-	-	-	114,609	**114,609**
Intangible assets	-	-	-	14,894	14,894
Investment in associate	-	-	-	172,776	**172,776**
Deferred tax asset	-	-	-	430,339	**430,339**
Balance due from group companies	-	-	-	403,525	**403,525**
Other assets	-	-	-	157,613	157,613
TOTAL ASSETS		**3,832,197**	**4,680,748**	**1,950,534**	**10,463,479**
Deposits from banking institutions	2.46%	1,295,754	-	-	**1,295,754**
Customer deposits	5.32%	4,768,596	3,267,988	-	**8,036,584**
Other liabilities	-	-	-	160,249	160,249
Share capital	-	-	-	1,503,238	1,503,238
Reserves	-	-	-	(532,346)	(532,346)
TOTAL LIABILITES		6,064,350	3,267,988	1,131,141	10,463,479
Asset – liability gap 2010		**(2,232,153)**	**1,412,760**	**819,393**	**-**

31 December 2009:	Effective interest rate %	3 months or less KShs'000	Between 3-12 months KShs'000	Non-interest bearing KShs'000	Total KShs'000
ASSETS					
Cash and balances with Central Bank of Kenya		-	-	306,044	**306,044**
Investments in Government securities	6.57%	-	692,051	-	**692,051**
Placements with other Banks	2.75%	-	408,111	-	**408,111**
Investment in Corporate Bond	12.50%	-	235,400	-	**235,400**
Loans and advances to customers	18.37%	1,972	1,951,327	-	**1,953,299**
Property and equipment	-	-	-	191,773	**191,773**
Intangible assets	-	-	-	7,374	**7,374**
Investment in associate	-	-	-	104,056	**104,056**
Deferred tax asset	-	-	-	313,339	**313,339**
Investment property	-	-	-	163,749	**163,749**
Other assets	-	-	-	103,391	**103,391**
Prepaid operating lease	-	-	-	12,788	12,788
TOTAL ASSETS		**1,972**	**3,286,889**	**1,202,514**	**4,491,375**
Deposits from Banking institutions	0.06%	15,000	-	-	**15,000**
Customer deposits	6.97%	3,602,285	705,411	-	**4,307,696**
Other liabilities	-	-	-	173,617	**173,617**
Share capital	-	-	-	461,622	**461,622**
Reserves	-	-	-	(466,560)	(466,560)
TOTAL LIABILITES		**3,617,285**	**705,411**	168,679	4,491,375
Asset – liability gap 2009		**(3,615,313)**	**2,581,478**	**1,033,835**	**-**

(d) Market risk (continued)

Sensitivity analysis on interest rates

An increase of 1 percentage point in interest rates for the period would have increased/(decreased) profit and loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. This analysis is performed on the same basis for 2009.

Effect in Kenya shillings thousands	Profit or loss 2010	Profit or loss 2009
Interest income	85,129	32,889
Interest expense	(93,323)	(43,227)
Net change in interest	**(8,194)**	**(10,338)**

A decrease of 1 percentage point in interest rates for the period would have had an equal but opposite effect on the profit and loss, on the basis that all other variables remain constant.

Currency risk

The Bank is exposed to currency risk through transactions in foreign currencies. The Bank's transactional exposures give rise to foreign currency gains and losses that are recognised in the profit or loss. In respect of monetary assets and liabilities in foreign currencies, the Bank ensures that its net exposure is kept to an acceptable level by buying and selling foreign currencies at spot rates when considered appropriate.

The various currencies to which the Bank is exposed at 31 December 2010 are summarised in the table below (all expressed in Kenya Shillings thousands):

31 December 2010 ON BALANCE SHEET ITEMS	USD	GBP	EURO	Total
ASSETS				
Cash and balances with Bank	206,821	74,000	46,205	327,026
Loans and advances to customers	372,453	3	161,840	534,296
Other assets	147,665	-	-	147,665
TOTAL ASSETS	**726,939**	**74,003**	**208,045**	**1,008,986**
Customer deposits	497,199	75,973	82,545	655,717
Borrowings	278,760	-	-	278,760
Other liabilities	3,014	275	212,871	216,160
TOTAL LIABILITIES	**778,973**	**76,248**	**295,416**	**1,150,637**
Net currency exposure – on balance sheet position	**(52,034)**	**(2,245)**	**(87,371)**	**(141,650)**
OFF BALANCE SHEET ITEMS LIABILITIES	**789,473**	**-**	**19,954**	**809,427**
Net currency exposure	**(841,507)**	**(2,245)**	**(107,325)**	**(951,077)**

31 December 2009:	USD	GBP	EURO	OTHER	Total
ON BALANCE SHEET ITEMS					
ASSETS					
Cash and balances with Bank	9,859	3,455	5,542	-	**18,856**
Loans and advances to customers	152,586	160,577	52,903	2,905	**368,971**
Other assets	33,510	-	-	-	**33,510**
TOTAL ASSETS	**195,955**	**164,032**	**58,445**	**2,905**	**421,337**
Customer deposits	231,697	163,879	23,490	42	**419,108**
Borrowings	15,000	-	-	-	**15,000**
Other liabilities	-	-	-	-	-
TOTAL LIABILITIES	**246,697**	**163,879**	**23,490**	**42**	**434,108**
Net currency exposure – on balance sheet position	**(50,742)**	**153**	**34,955**	**2,863**	**(12,771)**
OFF BALANCE SHEET ITEMS					
LIABILITIES	**40,149**	**-**	**-**	**-**	**40,149**
Net currency exposure	**(90,891)**	**153**	**34,955**	**2,863**	**(52,920)**

The following exchange rates were applied during the year:

	Average rate		Closing rates	
	2010	**2009**	**2010**	**2009**
US Dollar	79.47	77.37	80.80	75.85
Sterling Pound	122.58	121.45	124.74	121.97
Euros	104.71	107.95	107.21	108.96

Sensitivity analysis

A 10 percent increase in the rate of the Kenya shilling against the following currencies at 31 December would have increased/ (decreased) profit or loss for revaluation by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remains constant. The analysis is performed on the same basis for 2009.

Effect in Kenya shillings thousands	Profit or loss 2010	Profit or loss 2009
As at 31 December		
US Dollar	(5,203)	(5,074)
Sterling pound	(225)	15
Euros	(8,737)	3,496

A 10 percent decrease in the rate of the Kenya shilling against the above currencies at 31 December 2010 and 2009 would have had an equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

(e) Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This is supported by the development of overall standards for the management of operational risk in areas such as compliance with regulatory requirements, ethical and business standards, training and professional development, documentation of controls and procedures and requirements for the reconciliation and monitoring of transactions amongst others.

(f) Capital management

Regulatory capital
The Central Bank of Kenya sets and monitors capital requirements for the Bank. The Bank's operations are directly supervised by local regulators.

In implementing current capital requirements The Central Bank of Kenya requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. The Bank uses its internal grading as the basis for risk weightings for credit risk.

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

- Tier 1 capital, which includes ordinary share capital, share premium, perpetual bonds (which are classified as innovative Tier 1 securities), retained earnings, translation reserve and minority interests after deductions for goodwill and intangible assets, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.

- Tier 2 capital, which includes qualifying subordinated liabilities, statutory credit risk reserves and the element of the fair value reserve relating to unrealised gains on equity instruments classified as available-for-sale.

Various limits are applied to elements of the capital base. The amount of innovative tier 1 securities cannot exceed 15 percent of total tier 1 capital; qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying term subordinated loan capital may not exceed 50 percent of tier 1 capital. There also are restrictions on the amount of Statutory Credit Risk Reserve that may be included as part of tier 2 capital. Other deductions from capital include the carrying amounts of investments in subsidiaries that are not included in the regulatory consolidation, investments in the capital of Banks and certain other regulatory items.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

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

The Bank has complied with all externally imposed capital requirements throughout the period.

There have been no material changes in the Bank's management of capital during the period.

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

	2010 KShs'000	2009 KShs'000
Tier 1 capital		
Ordinary share capital	1,503,238	461,622
Retained earnings	(693,673)	(646,535)
	809,565	(184,913)
Tier 2 capital	76,802	78,352
Total regulatory capital	**886,367**	**(106,561)**
Risk-weighted assets		
On balance sheet risk weighted assets	5,669,759	2,310,128
Off balance sheet risk weighted assets	448,409	40,149
Total risk-weighted assets	**6,118,168**	**2,350,277**
Capital ratios		
Percentage of total regulatory capital to Risk-weighted assets	14.49%	(4.53) %
Minimum requirement	12.00%	12.00%
Percentage of core capital to risk weighted assets	13.23%	(7.87) %
Minimum requirement	8.00%	8.00%
Percentage of core capital to deposits	10.07%	(4.29) %
Minimum requirement	8.00%	8.00%

Capital allocation

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital, but in some cases the regulatory requirements do not reflect fully the varying degree of risk associated with different activities. In such cases the capital requirements may be flexed to reflect differing risk profiles, subject to the overall level of capital to support a particular operation or activity not falling below the minimum required for regulatory purposes. The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation, by the Risk Management Committee and Credit Committee, and is subject to review by the Board Audit Committee and the Board of Directors.

Although maximisation of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Bank to particular operations or activities, it is not the sole basis used for decision making. Account also is taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Bank's longer term strategic objectives. The Bank's policies in respect of capital management and allocation are reviewed regularly by the Board of Directors.

The CBK amended the Banking Act in 2009 which requires banks to increase their core capital as follows

Compliance date	Minimum Core Capital KShs
31 December 2010	500 million
31 December 2011	700 million
31 December 2012	1,000 million

The Bank is in compliance with the above requirements as at 31 December 2010.

5. USE OF ESTIMATES AND JUDGEMENTS

(a) Loan loss provisioning

The Group'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 either on an individual or on a portfolio 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. Impairment losses determined on a portfolio basis are assessed based on the probability of default inherent within the portfolio of impaired loans or receivables.

Estimating the amount and timing of future recoveries involves significant judgment, 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.

(b) Fair value of financial instruments

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

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

Subsequent to initial recognition, some of the Group's financial instruments are carried at fair value, with changes in fair value either reported within the profit or loss or within equity until the instrument is sold or becomes impaired. Details of the type and classification of the Group's financial instruments are set out in Note 6 to the financial statements.

(c) Depreciation of property and equipment

Critical estimates are made by the Directors in determining depreciation rates for property and equipment.

(d) Taxes

Determining income tax provisions involves judgment on the tax treatment of certain transactions. Deferred tax is recognised on tax losses not yet used and on temporary differences where it is probable that there will be taxable revenue against which these can be offset. Management has made judgments as to the probability of tax losses being available for offset at a later date.

6. FINANCIAL ASSETS AND LIABILITIES AND THEIR FAIR VALUES

(a) Accounting classifications and fair values

The table below sets out the group's classification of each class of financial assets and liabilities, and their fair values (excluding accrued interest):

As at 31 December 2010:	Held for trading KShs'000	Held to maturity KShs'000	Loans and receivables KShs'000	Available-for-sale KShs'000	Other amortised cost KShs'000	Total carrying amount KShs'000
Assets						
Cash and cash equivalents	-	-	656,778	-	-	656,778
Deposits and balances due from other banks	-	-	329,841	-	-	329,841
Investments in corporate bond	-	335,545	-	-	-	335,545
Investments in Government securities	-	2,996,145	-	-	-	2,996,145
Loans and advances to customers	-	-	4,851,414	-	-	4,851,414
Total assets	**-**	**3,331,690**	**5,838,033**	**-**	**-**	**9,169,723**
Liabilities and shareholders' funds						
Deposits and balances due to banking institutions	-	-	-	-	1,295,754	1,295,754
Customers' deposits	-	-	-	-	8,036,584	8,036,584
Total liabilities	**-**	**-**	**-**	**-**	**9,332,338**	**9,332,338**

As at 31 December 2009:						
Assets						
Cash and cash equivalents	-	-	306,044	-	-	306,044
Deposits and balances due from other banks	-	-	408,111	-	-	408,111
Investments in corporate bond	-	235,400	-	-	-	235,400
Investments in Government securities	-	692,051	-	-	-	692,051
Loans and advances to customers	-		1,953,299	-	-	1,953,299
Total assets	**-**	**927,451**	**2,667,454**	**-**	**-**	**3,594,905**
Liabilities and shareholders' funds						
Deposits and balances due to banking institutions	-	-	-	-	15,000	15,000
Customers' deposits	-	-	-	-	4,307,696	4,307,696
Total liabilities	**-**	**-**	**-**	**-**	**4,322,696**	**4,322,696**

(a) Accounting classifications and fair values (continued)

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

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.

Investments in Government securities and corporate bonds

Investments in Government securities and corporate bonds are carried at amortised cost using the effective interest rate method. The estimated fair value represents the discounted amount of future cash flows expected to be received. A substantial portion of investments in Government securities and corporate bonds mature within twelve months and hence the carrying amount is a good proxy of the fair value.

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 mature within 6 months and hence the carrying amount is a good proxy of the fair value.

7. INTEREST INCOME	Group 2010 KSHS'000	Group 2009 KSHS'000
Loans and advances to customers	506,540	361,215
Government securities	141,011	68,172
Placements with other banks	3,177	11,230
Corporate bonds	36,388	-
	687,116	**440,617**

8. INTEREST EXPENSE	2010 KSHS'000	2009 KSHS'000
Customer deposits	366,972	300,349
Deposits from other banks and banking institutions	24,221	8,785
	391,193	**309,134**

9. OTHER INCOME	2010 KSHS '000	2009 KSHS '000
Profit on sale of property and equipment	1,707	(354)
Bond Trading Income	147,457	-
Other income	31,033	14,496
	180,197	**14,142**

10. OPERATING EXPENSES	2010 KSHS '000	2009 KSHS '000
Salaries and employee benefits	238,385	215,667
Occupancy expenses	90,740	38,872
Deposit Protection Fund contribution	9,256	6,136
Intergration/Merger costs	142,805	-
Other expenses	253,783	198,723
	734,969	**459,398**

Included in other expenses are support services payable to a related company. During the year the Bank incurred costs of KShs 39,106,000.

11. STAFF COSTS

	Group 2010 KSHS'000	Group 2009 KSHS'000
Salaries and wages	203,206	158,315
Contributions to defined contribution scheme	10,324	8,914
Social security contributions	405	-
Staff welfare	24,450	48,438
	238,385	**215,667**
The average numbers of employees engaged during the year were:	172	148
Management staff	13	1
Unionisable	**185**	**149**

12. LOSS BEFORE TAXATION

	2010 KSHS'000	2009 KSHS'000
Loss before taxation is arrived at after charging/ (crediting):		
Depreciation expense	27,017	30,375
Amortisation of intangible assets	4,165	3,684
Directors' emoluments:		
Non-executives – Fees	1,677	3,257
Executives – Remuneration	11,990	16,343
Auditors' remuneration – Current year	4,200	2,500
(Gains)/Loss on sale of property and equipment	**(1,707)**	**354**

13. TAXATION

	2010 KSHS'000	2009 KSHS'000
Current tax at 30% on adjusted profit for tax purposes	-	-
Deferred tax credit	(51,058)	(159,593)
Prior year understatement of deferred tax asset	(18,473)	-
Tax credit for the year(Note 24)	**(69,531)**	**(159,593)**

The tax on the Bank's loss differs from the theoretical amount using the basic tax rate as follows:	2010 KSHS'000	2009 KSHS'000
Accounting loss before tax	**(137,596)**	**(729,552)**
Computed tax using the applicable tax rate of 30%	(41,278)	(218,866)
Non-deductible expenses and non-taxable income	(9,780)	59,273
Prior year understatement of deferred tax asset	(18,473)	-
Income tax expense	**(69,531)**	**(159,593)**

14. BASIC AND DILUTED EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is based on:	Group 2010	Group 2009
Net loss for the year attributable to shareholders – KShs'000	(68,063)	(569,959)
Weighted average number of ordinary shares in issue at 31 December	214,464	92,324
Basic and diluted earnings per share	(0.32)	(6.17)

15. DIVIDENDS PER SHARE

No dividends were declared in 2010 (2009 - Nil).

16. CASH AND BALANCES WITH CENTRAL BANK OF KENYA

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Cash on hand	111,314	91,210
Balances with Central Bank of Kenya:		
- Cash reserve ratio	365,134	190,941
- Other	180,330	23,893
	656,778	**306,044**

The cash ratio reserve with Central Bank of Kenya (CBK) is non-interest earning and is based on the value of deposits as adjusted for CBK requirements. At 31 December 2010, the cash reserve ratio requirement was 4.5% of eligible deposits (2009 – 4.5%). The funds are not available to finance the Bank's day-to-day operations.

17. INVESTMENTS HELD TO MATURITY

Government securities	Group and Company 2010 **KShs'000**	Group and Company 2009 **KShs'000**
Treasury bills – due after 90 days	148,900	-
Treasury bonds	2,847,245	692,051
	2,996,145	692,051
Corporate bonds	335,545	235,400
Total investments	**3,331,690**	**927,451**

The weighted average effective interest rate on government securities for the year 2010 was 6.33% (2009 - 6.57%).
The weighted average effective interest rate on corporate bond for the year 2010 was 12.5% (2009 – 12.5%).

18. PLACEMENTS WITH OTHER BANKS

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Due within 90 days	**329,841**	**408,111**

The weighted average effective interest rate on placements with other banks for the year 2010 was 2.74% (2009 - 2.75%).

19. LOANS AND ADVANCES TO CUSTOMERS

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
(a) Overdrafts	2,416,908	945,498
Loans	2,566,315	1,213,351
Bills discounted	36,394	19,572
Others	317,671	247,710
Gross loans and advances	5,337,288	2,426,131
Less: Provisions for impairment losses on loans and advances	(485,874)	(472,832)
Net loans and advances	**4,851,414**	**1,953,299**

(b) **Impairment losses on financial assets**

31 December 2010:	Specific impairment losses KShs'000	Portfolio impairment losses KShs'000	Total KShs'000
At 1 January 2010	472,832	-	472,832
Acquisition through business combination	62,945	4,790	67,735
Amounts written off during the year	(130,124)	-	(130,124)
	405,653	4,790	410,443
Provisions made during the year	66,977	8,455	75,432
At 31 December 2010	**472,630**	**13,245**	**485,875**
31 December 2009:			
At 1 January 2009	257,437	-	257,437
Amounts written off during the year	(86,650)	-	(86,650)
	170,787	-	170,787
Provisions made during the year	302,045	-	302,045
At 31 December 2009	**472,832**	**-**	**472,832**

The weighted average effective interest rate on loans and advances to customers for the year 2010 was 11.41% (2009 – 18.37%).

(c) **Non performing loans and advances**

Loans and advances include an amount of KShs 1,198,108 (2009 – KShs 993,590) which has been classified as impaired. These loans have been written down to their recoverable amount.

20. PROPERTY AND EQUIPMENT

2010:	Leasehold improvements & buildings KShs'000	Motor vehicles KShs'000	Furniture fixtures & fittings KShs'000	Computer equipment KShs'000	Office equipment KShs'000	Total KShs'000
Cost:						
At 1 January 2010	141,250	22,425	76,876	57,093	103,913	401,557
Acquisition through business combination	11,091	1,994	8,212	8,625	5,781	35,703
Additions	9,615	-	42,751	8,343	6,263	66,972
Disposals	(150,865)	(18,442)	(8,340)	(12,404)	(11,324)	(201,375)
At 31 December 2010	11,091	5,977	119,499	61,657	104,633	302,857
Depreciation:						
At 1 January 2010	-	18,721	54,617	51,148	85,298	209,784
Charge for the year	778	1,670	5,627	5,094	13,848	27,017
Disposals	-	(16,485)	(8,340)	(12,404)	(11,324)	(48,553)
At 31 December 2010	778	3,906	51,904	43,838	87,822	188,248
Net book value:						
At 31 December 2010	**10,313**	**2,071**	**67,595**	**17,819**	**16,811**	**114,609**

2009:						
Cost:						
At 1 January 2009	-	24,025	60,596	54,242	102,898	241,761
Additions	-	-	16,280	2,851	1,015	20,146
Reclassifications	73,518	-	-	-	-	73,518
Revaluation Surplus	67,732	-	-	-	-	67,732
Disposals	-	(1,600)	-	-	-	(1,600)
At 31 December 2009	141,250	22,425	76,876	57,093	103,913	401,557
Depreciation:						
At 1 January 2009	-	15,369	49,041	45,560	70,239	180,209
Charge for the year	-	4,152	5,576	5,588	15,059	30,375
Disposals	-	(800)	-	-	-	(800)
At 31 December 2009	-	18,721	54,617	51,148	85,298	209,784
Net book value:						
At 31 December 2009	**141,250**	**3,704**	**22,259**	**5,945**	**18,615**	**191,773**

21. INTANGIBLE ASSETS	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Cost		
At 1 January	25,600	17,614
Acquisition through business combination	10,158	-
Additions in the year	1,527	7,986
Disposals	(4,017)	-
At 31 December	33,268	25,600
Amortisation		
At 1 January	18,226	14,542
Disposals	(4,017)	-
Charge for the year	4,165	3,684
At 31 December	18,374	18,226
Net book value	**14,894**	**7,374**

22. PREPAID OPERATING LEASE

Prepaid operating lease rentals are recognised at historical cost

The movement in prepaid operating lease rentals is as follows:	2010 KShs'000	2009 KShs'000
Cost as at 1 January	12,788	-
Disposal	(12,788)	-
Transfer from capital work-in-progress	-	12,788
Cost at 31 December	**-**	**12,788**

The leasehold land was acquired in 2009 and sold to the Parent company in 2010.

23. INVESTMENTS IN ASSOCIATE COMPANIES

The Bank's share of profit of its equity accounted investees for the year was KShs 38,720,000 (2009 – KShs 25,955,000).

The following is the movement in the Bank's investment in the associates:	2010 KShs'000	2009 KShs'000
Balance as at 1 January	104,056	78,101
Acquired through business combination	30,000	-
Share of profit of associates	38,720	25,955
Net investment in associates	**172,776**	**104,056**

Summary financial information for equity accounted investees, not adjusted for the percentage ownership held by the group:

	Ownership	Current assets KShs'000	Non-Current assets KShs'000	Total assets KShs'000	Current liabilities KShs'000	Equity &Non-current liabilities KShs'000	Total Equity & liabilities KShs'000	Revenues KShs'000	Expenses KShs'000	Profit/ (loss) KShs'000
2010:										
Equatorial Investment Bank	20%	100,798	20,572	121,370	3,759	117,611	121,370	8,761	20,427	(11,666)
Fidelity Shield Insurance Company	23.86%	288,843	1,251,906	1,540,749	171,905	1,368,844	1,540,749	295,891	123,833	172,058
2009:										
Fidelity Shield Insurance Company	24.42%	295,605	941,966	1,237,571	139,312	1,098,259	1,237,571	239,193	122,285	116,908

24. DEFERRED TAX

Deferred tax assets at 31 December 2010 and 2009 are attributable to movements in temporary differences between calculations of certain items for accounting and for taxation purposes as specified below:

Group and Company

2010:	Balance at 01/01/2010 KShs'000	Acquisition during the year KShs'000	Credited to equity KShs'000	Credited to profit & loss KShs'000	Balance at 31/12/2010 KShs'000
Arising from:					
Plant and equipment	12,136	-	-	(4,584)	7,552
Carried forward tax loss	342,852	-	-	(77,622)	265,230
General provisions for loans and advances	-	21,642	-	124,120	145,762
Revaluation Surplus	(20,320)	-	20,320		-
Fair Value gain on investment property	(23,233)	-	-	23,233	-
Other provisions	1,904	5,507	-	4,384	11,795
	313,339	**27,149**	**20,320**	**69,531**	**430,339**

Group and Company

2009:	Balance at 01/01/2009 KShs'000	Charged to other comprehensive income KShs'000	Credited to profit & loss KShs'000	Balance at 31/12/2009 KShs'000
Arising from:				
Plant and equipment	7,131	-	5,005	12,136
Tax loss carried forward	165,855	-	176,997	342,852
Revaluation Surplus	-	(20,320)	-	(20,320)
Fair Value gain on investment property	-	-	(23,233)	(23,233)
Other provisions	1,080	-	824	1,904
	174,066	**(20,320)**	**159,593**	**313,339**

25. INVESTMENT PROPERTY

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Balance at 1 January	163,749	65,000
Transfer from property and equipment	-	86,305
Change in fair value	-	77,444
Disposal during the year	(163,749)	(65,000)
	-	163,749

26. BALANCE DUE FROM PARENT COMPANY

The balance due from the Parent Company represents amounts owed to the bank by Equatorial Commercial Holding Limited.

	2010 KShs'000	2009 KShs'000
Investment Property	327,273	-
Capital Work in Progress	76,252	-
	403,525	-

27. OTHER ASSETS

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Deposits and prepayments	34,440	77,430
Capital Work in Progress	16,412	25,961
Items in transit	106,761	-
	157,613	103,391

28. CUSTOMER DEPOSITS

From private sector & individuals	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Non-profit institutions and individuals	2,009,997	2,240,726
Private enterprises	5,371,174	1,770,290
Foreign currency accounts	655,413	296,680
	8,036,584	4,307,696

Included in customers' deposits is KShs 340,187,885 (2009 – KShs 39,861,000) due to related companies. Interest paid on such deposits during the year amounted to KShs 49,788,134 (2009 – KShs 4,591,000).

29. OTHER LIABILITIES

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Bills payable	91,442	125,415
Sundry creditors	68,807	48,202
	160,249	173,617

30. SHARE CAPITAL AND RESERVES

(a) Share capital

	2010 KShs'000	2009 KShs'000
Authorised		
300,647,555 (2009:-92,324,155) Ordinary shares of KShs 5 each	1,503,238	461,622
Issued and fully paid		
300,647,555 (2009:-92,324,155) Ordinary shares of KShs 5 each	1,503,238	461,622

The movement in share capital is as follows:	2010 KShs'000	2009 KShs'000
As at 1 January	461,622	461,622
Issued on business combination	1,041,616	-
	1,503,238	461,622

(b) Statutory credit risk reserve

Where impairment losses required by legislation or regulations exceed those computed under International Financial Reporting Standards (IFRSs), the excess is recognised as a statutory reserve and accounted for as an appropriation of retained profits. These reserves are not distributable.

31. ACQUISITION THROUGH BUSINESS COMBINATION

On 31 May 2010, Equatorial Commercial Bank Limited (ECB) and Southern Credit Banking Corporation Limited (SCBC) executed an asset and portfolio (business) transfer agreement for the transfer of ECB banking business to SCBC who paid a fair consideration for transfer of the business by issue of new shares in equal value to the assets and liabilities transferred as outlined below (details of the merger transactions are highlighted in the summary of directors report on merger transactions on page 7 of this financial statements).

Merger at 31 May 2010	**Carrying amounts KShs'000**	**Fair value adjustments KShs'000**	**Recognised value KShs'000**
Assets			
Cash acquired:			
Cash and Balances with Central Bank of Kenya	48,736	-	48,736
Local bank deposits	544,780	-	544,780
Foreign bank deposits	511,303	-	511,303
Balances due to Central Bank	(159,930)	-	(159,930)
Deposits from banking Institutions	(553,115)	-	(553,115)
Total cash acquired	**391,774**	**-**	**391,774**
Other assets and liabilities acquired:			
Cash ratio reserve	159,853	-	159,853
Government securities	1,707,359	-	1,707,359
Corporate bond	93,200	-	93,200
Loans and advances (net)	2,513,401	-	2,513,401
Investments in associate companies	30,000	-	30,000
Property and equipment	35,703	-	35,703
Intangible assets	10,158	-	10,158
Deferred tax asset	27,149	-	27,149
Other assets	55,767	-	55,767
Customer deposits	(3,916,056)	-	(3,916,056)
Tax payable	(17,538)	-	(17,538)
Other liabilities	(49,154)	-	(49,154)
Total other assets and liabilities acquired	**649,842**	**-**	**649,842**
Net identifiable assets and liabilities	**1,041,616**	**-**	**1,041,616**
Consideration satisfied by issue of shares			1,041,616
Net cash outflow			-

32. NOTES TO THE CASH FLOW STATEMENT

(a) Reconciliation of loss before taxation to cash flows from operating activities

	2010 KShs'000	2009 KShs'000
Loss before taxation	(137,595)	(729,552)
Share of profit of associates	(38,720)	(25,955)
Other income	-	(59,911)
Depreciation	27,017	30,375
Amortisation of intangible assets	4,165	3,684
Profit on disposal of property and equipment	(1,707)	-
Net cash outflow from trading activities	**(146,840)**	**(781,359)**
(Decrease)/increase in operating assets		
Central Bank of Kenya cash reserve	(14,340)	(2,709)
Investment in government securities maturing after 90 days	(596,735)	76,918
Loans and advances to customers	(402,756)	735,610
Investment in corporate bonds	(6,945)	-
Balances due from Parent company	(76,123)	-
Other assets	1,545	67,833
	(1,095,354)	**877,652**
Increase/(decrease) in operating liabilities		
Customers deposits	(187,168)	202,001
Other liabilities	(80,060)	30,466
	(267,228)	**232,467**
Net cash outflow from operations	**(1,509,422)**	**328,760**
Tax paid	-	-
Net cash flow from operating activities	**(1,509,422)**	**328,760**

(b) Analyses of the balance of cash and cash equivalents

	Group 2010 KShs'000	Group 2009 KShs'000	Change in the year KShs'000
Cash and balances with Central Bank of Kenya	291,644	115,103	(176,541)
Balances due from Banking institutions	329,841	408,111	78,270
Deposits and Balances due to banking Institutions	(1,295,754)	(15,000)	1,280,754
	(674,269)	**508,214**	**1,182,483**

33. RETIREMENT BENEFIT OBLIGATIONS

The Bank contributes to a provident fund established for the benefit of its employees. This scheme is classified as a defined contribution scheme, whereby the Bank matches contributions to the fund made by employees at; 5% (former ECB) and 7.5% (former SCBC) of the employee's basic salary. During the year, the Bank incurred costs of KShs 10,457,887 as contributions payable (2009 – KShs 8,914,000).

34. CONTINGENT LIABILITIES

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. The amounts reflected in the table for guarantees and letters of credit represent the maximum accounting loss that would be recognised at the reporting date if counter parties failed completely to perform as contracted.

	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Commitments with respect to:		
Irrevocable letters of credit	51,192	54,207
Guarantees	508,569	-
Acceptances	922	302,390
Inward foreign documentary bills	190,239	-
Forward deals outstanding	195,617	-
	946,539	**356,597**

Nature of contingent liabilities

Letters of credit commit the Bank to make payments to third parties, on production of documents, which are subsequently reimbursed by the customers.

Guarantees are generally written by a Bank to support performance by a customer to third parties. The Bank will only be required to meet these obligations in the event of the customers default.

An acceptance is an undertaking by the Bank to pay a bill of exchange drawn on a customer. The Bank expects most of the acceptances to be presented, and reimbursement by the customer is almost immediate.

Bills for collection are cheques, drawn against foreign or local Banks, deposited by the Bank's customers, which are in the process of clearing with the correspondent Banks.

Inward foreign documentary bills are extended by the Bank to its customers to enable them import goods from overseas suppliers. The Bank however does not pay the exporters if the importer does not meet his/her contractual obligations.

35. ASSETS PLEDGED AS SECURITY

	Group and Company 2010	Group and Company 2009
Cash pledged to Central Bank domestic foreign currency clearing	**USD 100,000**	**USD 100,000**

The above funds pledged as security are not available to finance the Bank's day-to-day operations.

36. RELATED PARTY TRANSACTIONS

The Bank has entered into transactions with some of its directors, affiliates and employees:

The aggregate amount of loans:	**Group and Company 2010 KShs'000**	**Group and Company 2009 KShs'000**
Directors and affiliates		
Balance at the beginning of the year	14,965	75,745
Loans advanced during the year	58,145	65,460
Interest charged during the year	5,613	16,841
Loans repayments received	(10,621)	(143,081)
	68,102	**14,965**
Guarantees	**7,377**	**7,037**

The loans to related parties were given on commercial terms and conditions. The related interest income in the year was KShs 58,272,969 (2009 – KShs 10,507,400).

	Group and Company 2010 KShs'000	**Group and Company 2009 KShs'000**
Employees:		
Balance at the beginning of the year	30,790	64,860
Loans advanced during the year	17,865	-
Loans repayments received	(8,139)	(34,070)
	40,516	**30,790**
Guarantees	**100**	**-**

The related interest income in the year was KShs 3,780,231.

37. OPERATING LEASE

Operating lease rentals are payable as follows:	Group and Company 2010 KShs'000	Group and Company 2009 KShs'000
Tenancy:		
Less than one year	51,970	1,675
Between one and five years	117,157	14,081
Due after five years	8,053	29,394
	177,180	**45,150**

The Bank leases a number of Bank premises under operating leases. The leases typically run for an initial period of between five and eight years with an option to renew the lease after that date. None of the leases include contingent rentals. During the year ended 31 December 2010, KShs 49,322,528 (2009 – KShs 33,610,000) was recognised as an expense in the profit or loss in respect of operating leases.

The head office is leased from a related company for a period of five years, three months until 31 March 2012. The amount paid during the year in respect of head office lease was KShs 25,264,800 (2009 – KShs 21,339,560).

38. CAPITAL COMMITMENTS

There are no authorised capital commitments that are outstanding at the year end.

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