DRIVING SUSTAINABILITY THROUGH PEOPLE AND INNOVATION

2017 ANNUAL REPORT & FINANCIAL STATEMENTS

BRITISH AMERICAN TOBACCO
KENYA

BRITISH AMERICAN TOBACCO KENYA PLC
ANNUAL REPORT AND FINANCIAL STATEMENTS 2017

This is the Annual Report and Financial Statements (Annual Report) of British American Tobacco Kenya plc (BAT Kenya), comprising the Strategic Report, the Governance Report and the Audited Financial Statements for the year ended 31 December 2017. This Annual Report has been drawn up and is presented in accordance with, and reliance upon applicable Kenyan Company Law and the Companies Act, 2015. The liabilities of the Directors in connection with this Report shall be subject to the limitations and restrictions provided by such law.

A printed copy of the Annual Report is mailed to shareholders on the mail register who have elected to receive it. The Report is also emailed to those shareholders who have at any previous time indicated their email addresses. References in this publication to 'BAT Kenya', 'we', 'us' and 'our' when denoting opinion or tobacco business refer to British American Tobacco Kenya plc.

CAUTIONARY STATEMENT

The material in this Annual Report is provided for the purpose of giving information about BAT Kenya to adult shareholders and is not provided for tobacco product advertising, promotional or marketing purposes. This material does not constitute and should not be construed as constituting an offer to sell or a solicitation of an offer to buy any of our tobacco products. Our products are sold in compliance with the law.

The Strategic Report and certain other sections of the Annual Report contain forward-looking statements that are subject to risk factors associated with, amongst other things, the changing economic and business dynamics affecting the Kenyan and export markets. It is believed that the expectations reflected in these statements are reasonable but they may be affected by a wide range of variables that could cause actual results to differ materially from those currently anticipated.

ABOUT US

BAT Kenya is a strong company with a rich heritage that spans over 100 years. We have over ten cigarette brands sold in the Kenyan market, which are chosen by a majority of Kenya's adult smokers. Our diverse strengths, including our heritage, our innovative brands, our talented people and best in class processes and ways of working, are the foundations of our continuing progress. We are a forward-looking company with a proven strategy which we continue to improve in order to deliver value for our shareholders. We are confident that our investment in the Kenyan market will ensure that we continue to achieve sustainable growth today and in the future.

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George Maina | Chairman
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NOTICE OF THE 2018 ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the Sixty-Sixth Annual General Meeting of British American Tobacco Kenya plc will be held in the Mara Ball Room, Hotel Intercontinental, Nairobi, on Friday 11 May 2018, at 11:00 a.m. for the following purposes:-

Ordinary business

1. To receive, consider and if approved, adopt the Company's audited financial statements for the year ended 31 December 2017, together with the reports of the Chairman, Directors, and Auditors thereon.
2. To confirm the interim dividend of KSh. 3.50 per ordinary share paid on 21 September 2017 and to declare a final dividend of KSh. 22.50 per ordinary share payable, net of Withholding Tax, on 11 May 2018 to Shareholders on the register at the close of business on 16 March 2018.
3. To elect Directors:
   i. Beverley Spencer-Obatoyinbo and Sidney Wafula retire and being eligible, offer themselves for re-election in accordance with Article 102 of the Articles of Association.
   ii. George Maina, Carol Musyoka and Gayling May retire by rotation and being eligible, offer themselves for re-election in accordance with Article 103 of the Articles of Association.
4. To approve the remuneration of Directors and the Directors' Remuneration Report for the year ended 31 December 2017.
5. To reappoint KPMG Kenya to continue in office as External Auditors of the Company by virtue of Section 721 (2) of the Companies Act, 2015 and to authorise the Directors to fix their remuneration.

By Order of the Board
Ruth Ngobi
Company Secretary
P.O. Box 30000-00100
Likoni Road
Nairobi

15 February 2018

NOTES:

1. Any Member who is entitled to attend and vote at the Annual General Meeting is entitled to appoint a proxy to attend and vote in his/her stead. Such proxy need not be a member of the Company. A proxy form is provided with the Annual Report and can also be obtained from the Company's website, www.batkenya.com.
2. Shareholders who do not propose to be at the Annual General Meeting are requested to complete and return the form to The Co-operative Bank of Kenya Limited, Registrars Services, 1 Floor CIC Plaza II, Mara Road, Upper Hill, Nairobi P. O. Box 48231-00100 Nairobi, or alternatively to the Registered Office of the Company so as to arrive not later than 2:30 p.m. on 9 May 2018. Duly signed proxy forms may also be emailed to shares@co-opbank.co.ke in PDF format.
3. In accordance with the Company's Articles of Association, a copy of the entire Annual Report and Financial Statements may be viewed and/or downloaded from the Company's website, www.batkenya.com.

EXPLANATORY NOTES TO **RESOLUTIONS TO BE PASSED**

Agenda Item 1 - Report and Financial Statements 2017

Resolution 1:

THAT the Report of the Directors and the Financial Statements for the year ended 31 December 2017, as audited and reported by the Company's Auditors, now submitted to this meeting, be and are hereby approved and adopted.

The Report and Financial Statements are for the year ended 31 December 2017.

Agenda Item 2 - Declaration of Final Dividend

Resolution 2:

THAT the interim dividend of KSh. 3.50 per Ordinary Share paid on 21 September 2017 be and is hereby confirmed and that a final dividend of KSh. 22.50 per ordinary share payable, net of Withholding Tax, on 11 May 2018 to Shareholders on the Register at the close of business on 16 March 2018 be and is hereby approved.

The Company paid an interim dividend of KSh. 3.50 per Ordinary Share on 21 September 2017. The Board recommends a final dividend of KSh. 22.50 per Ordinary Share, bringing the total dividend for the year to KSh. 26 per Ordinary Share. Subject to approval by Shareholders, the final dividend will be paid on 11 May 2018 to Shareholders on the Register on 16 March 2018.

Agenda Item 3 - Directors seeking re-election

Resolution 3:

THAT the re-election of all retiring Directors as set out in Agenda Item 3 and in the Director's Report, be dealt with by a single resolution.

In accordance with Section 132(1) of the new Companies Act, 2015, if the Shareholders agree, the retiring Directors may be re-elected by a single resolution. This Resolution seeks Shareholders consent to re-elect eligible Directors by a single resolution.

Agenda Item 3 - Directors seeking re-election

Resolution 4:

THAT Beverley Spencer-Obatoyinbo, Sidney Wafula, George Maina and Carol Musyoka be and are hereby re-elected Directors of the Company.

Beverley Spencer-Obatoyinbo and Sidney Wafula, seek re-election in accordance with Article 102 of the Company's Articles of Association following their appointment as Managing Director and Finance Director respectively on 2 May 2017.

In relation to the re-election of George Maina, Carol Musyoka and Gayling May as Non-Executive Directors, it is hereby confirmed that the Nominations Committee and the Board determined that each of them continues to perform effectively and demonstrates commitment to their roles, and that all three are influential individuals in their respective fields and backgrounds.

Their balance of knowledge and skills combined with their diversity and business experience makes a major contribution to the proper functioning of the Board and its Committees. Biographical details of the directors seeking re-election are set out on pages 38 to 42 of this Annual Report.

Copies of the Directors' letters of appointment are available for inspection during normal business hours at the Company's registered office on any business day.

Agenda Item 4 - Directors' Remuneration

Resolution 5:

THAT the Directors' remuneration and Directors' Remuneration Report be and are hereby Approved.

Resolution 5 is an advisory vote to approve the Directors' remuneration and Directors' Remuneration Report as prescribed by the CMA Code of Corporate Governance Practices for Issuers of Securities to the Public.

The Remuneration Report is set out on pages 62 to 64 of this Annual Report.

Agenda Item 5 - Re-appointment of Auditors and Auditors' Remuneration

Resolution 6:

THAT in accordance with Section 721 (2) of the Companies Act, 2015, KPMG Kenya is reappointed to continue in office as the Auditor of the Company and that the Directors be and are hereby authorised to fix their remuneration.

With KPMG having expressed their willingness to continue in office as the Companies External Auditors in accordance with the provisions of Section 721 (2), it is proposed that the Directors be authorised to fix Auditors' remuneration for the ensuing financial year.

CORPORATE **INFORMATION**

Board of Directors

George Maina*	(Chairman)
Beverley Spencer-Obatoyinbo	(Managing Director)
Sidney Wafula	(Finance Director)
Gayling May*	
Carol Musyoka*	
Mahmud Jan Mohamed*	
Teddy Mapunda*	
Peter Mwangi*	
Dr. Martin Oduor-Otieno*	
Ruth Ngobi	(Company Secretary)

Audit, Governance and Corporate Social Responsibility Committee

Dr. Martin Oduor-Otieno*	(Chairman)
Gayling May*	
Carol Musyoka*	
Mahmud Jan Mohamed*	
George Maina*	(By Invitation)
Beverley Spencer-Obatoyinbo	(Permanent invitee)
Sidney Wafula	(Permanent invitee)
Seyi Adeyemo	(Permanent invitee)
Simukai Munjanganja	(Permanent invitee)
Cindy Albertyn	(Secretary)

Nominations Committee

George Maina*	(Chairman)
Gayling May*	
Peter Mwangi*	
Mahmud Jan Mohamed*	
Beverley Spencer-Obatoyinbo	(Permanent invitee)
Ruth Ngobi	(Secretary)

Remuneration Committee

Peter Mwangi*	(Chairman)
Teddy Mapunda*	
Carol Musyoka*	
Beverley Spencer-Obatoyinbo	(Permanent invitee)
Sidney Wafula	(Permanent invitee)
Razeeah Belath	(Secretary)

* Non-Executive Directors

Auditors

KPMG Kenya
Certified Public Accountants of Kenya
ABC Towers, 8th Floor
ABC Place, Waiyaki Way
P.O. Box 40612-00100
NAIROBI

Corporate Governance Auditor

Dorion Associates
Thompson Estate, Diani Close
Off Ole Odume Road
P.O Box 29737 - 00202
NAIROBI

Registrar

The Co-operative Bank of Kenya Limited
Registrar Services
1st Floor, CIC Plaza B
Mara Road, Upper Hill
P.O. Box 48231-00100
NAIROBI

Principal Advocates

Hamilton Harrison & Mathews
Wing A, 1st floor
Delta Office Suites
Waiyaki Way
P.O Box 30333-00100
NAIROBI

Kaplan & Stratton
Williamson House
4th Ngong Avenue
P.O. Box 40111-00100
NAIROBI

Principal Bankers

Barclays Bank of Kenya Limited
Citibank NA
Commercial Bank of Africa Limited
Standard Chartered Bank Kenya Limited

Secretary and Registered Office

Ruth Ngobi
BAT Kenya offices
Likoni Road, Industrial Area
P.O. Box 30000-00100
NAIROBI

CHAIRMAN'S **STATEMENT**

> "Our domestic business continues to feel the effects of the sudden 50% excise increase in December 2015, with the resulting price increase having led to increased incidence of illicit trade especially in Western Kenya."

George Maina Chairman

Introduction

Welcome to our Annual Report for 2017. I am very pleased to report that the Company delivered solid results, despite a particularly challenging trading environment in Kenya and across our export markets.

A difficult trading environment

In Kenya, inflation peaked at 11.7% in May 2017 and stabilised at circa 5% by the end of 2017. September 2017 saw the first full year of the implementation of the Kenya Banking Amendments 2016 Act, which among other things capped bank lending rates.

This has resulted in lower lending to SMEs and the public, adversely impacting money circulation. This was exacerbated by the prolonged electioneering period in Kenya, all of which have resulted in significantly lower consumer disposable income.

Our export markets have not been spared. In the Democratic Republic of Congo, the local currency depreciated by 36% versus the USD and civil conflict persists due to political uncertainty. In Somalia, drought, insecurity and devaluation put pressure on the economy. Egypt continues to feel the effect of the sudden currency devaluation in November 2016.

The regulatory environment and illicit trade

A stable regulatory and taxation environment remains a key enabler for our success. We continue engaging Governments on the importance of easing and harmonising trade within the East African Community (EAC), while ensuring that stable and predictable taxation regimes prevail.

The domestic business continues to feel the effects of the sudden 50% excise increase in December 2015. The resulting price increase has led to increased incidence of illicit trade duty not paid product and product containing counterfeit tax stamps), especially in Western Kenya.

The introduction in April 2017 of an unjustified 87% increase in the cost of tax stamps puts further pressure on our costs. The introduction of discriminatory excise regimes and maintenance of non-tariff barriers within the EAC has posed more challenges with regard to expansion of export products from the BAT Kenya manufacturing hub. We continue to actively engage Governments across the markets to lift these barriers to trade and conform to the treaty.

Developments within the Common Market for Eastern and Southern Africa (COMESA), particular accession of Free Trade Agreements, continue to be a focus area. Eliminating tariff barriers would drive market access and growth for our business and most especially manufacturing.

Business performance

The challenging operating environment impacted our ability to grow the topline. Net revenue declined by 6%, driven by lower domestic revenues as consumer disposable income declined. Notable gains were made in the export markets where we grew revenue and profitability.

However, the growth in export markets could not offset the decline in the domestic business. This decline, together with the unexpected increase in tax stamp costs and higher reorganisation and financing costs, drove an 18% decline in profit before tax.

Dividends

The Board of Directors recommend a final dividend of KSh. 22.50 per share for 2017, payable net of Withholding Tax on 11 May 2018 to shareholders on the register on 16 March 2018. This reflects the confidence in the sustainability of our business.

This takes the total dividend for 2017 to KSh. 26.00 per share (2016: KSh 43.00 per share).

Changes to the Board of Directors

The current memberships of the Company's Board committees can be found on pages 52 to 53.

On behalf of the Board, I would also like to thank our Company Secretary, Ruth Ngobi, who will leave immediately after the Annual General Meeting in May 2018, following 16 years in the role. Replacing Ruth is Head of Legal, Waeni Ngea, who was appointed as Company Secretary Designate with effect from 15 February 2018 and will become Company Secretary effective from 12 May 2018.

Outlook

While challenging trading conditions are likely to continue in the immediate future, I am confident that the Company has excellent long-term prospects. My Board has full confidence in its strategy to deliver high-quality innovative products to consumers at affordable prices while continuing to invest in developing high calibre people.

On behalf of the board, I would like to thank the employees, suppliers, government agencies and other stakeholders for their efforts in ensuring the business delivers solid results. I look forward to their help as we work to ensure that the business recovers to generate growth in shareholder value in the years ahead.

George Maina
Chairman

TAARIFA YA MWENYEKITI

George Maina Mwenyekiti

> "Biashara yetu inaendelea kuathirika na kuongezwa ghafla kwa asilimia 50 ya ushuru unaotozwa sigara hapa nchini tangu mwezi wa Disemba 2015, matokeo yake yakiwa kuongezeka kwa bei ya sigara, ambayo imesababisha kuchipuka kwa biashara haramu, hasa katika sehemu za Magharibi mwa Kenya."

Utangulizi

Karibu kwa ripoti yetu ya biashara kwa kipindi cha mwaka 2017. Ni furaha yangu kuwajulisha kwamba kampuni ilinakili matokeo thabiti licha ya changamoto ya mazingira ya biashara, sio tu hapa nchini bali pia katika masoko yetu ya nje.

Mazingira magumu ya biashara

Hapa nchini Kenya, gharama ya maisha iliongezeka na kufika asilimia 11.7 mwezi wa Mei 2018, japo ilipungua hadi asilimia 5 kufikia mwisho wa mwaka huo. Mwezi wa Septemba mwaka 2017, ulikuwa mwaka moja kamili tangu marekebisho ya sheria kuhusu sekta ya benki (Kenya Banking Ammendments 2016 Act) yalipoanza kutekelezwa, marekebisho ambayo miongoni mwa mambo mengine, yaliweka kiwango cha riba kinachotozwa mikopo na benki.

Hii ilisababisha kupungua kwa mikopo inayotolewa kwa biashara ndogo ndogo na zile za kadri, na hivyo kuathiri usambazaji wa pesa. Hali hiyo ilizidishwa na kipindi kirefu cha kampeni za uchaguzi hapa nchini, na kusababisha wakenya wengi kukosa mapato ya matumizi ya kila siku

Masoko yetu ya nje hayakusazwa na hali hiyo. Katika jamhuri ya kidemokrasia ya Congo (DRC) kwa mfano, thamani ya sarafu ya nchi hiyo ilipungua kwa asilimia 36 dhidi ya dola ya Marekani, huku mvutano wa kisiasa ukiendelea kusakama nchi hiyo. Katika nchi ya Somalia, ukame, utovu wa usalama na kupungua kwa thamani ya sarafu ya nchi hiyo, navyo viliendelea kuongeza shinikizo kwa uchumi wa nchi hiyo, huku Misri nayo ikihisi athari za kupungua kwa thamani ya sarafu yake kuliko tekelezwa mwezi Novemba mwaka 2016.

Mazingira ya uthibiti na biashara haramu

Mfumo imara wa uthibiti na utozaji ushuru ni kigezo muhimu kwa ufanisi wa biashara yetu. Kwa hivyo tunaendelea kushauriana na serikali kuhusu umuhimu wa kuwianisha mifumo ya biashara katika nchi yanachama wa Jumuiya ya Afrika Mashariki (EAC) na wakati huo huo kuhakikisha kuna viwango vinavyo bashirika vya ushuru.

Biashara yetu hapa nchini inaendelea kuathirika na kuongezwa ghafla kwa asilimia 50 ushuru unaotozwa kwa sigara hapa nchini, tangu mwezi Disemba mwaka 2015, matokeo yake yakiwa kuongezeka kwa bei ya sigara, ambayo imesababisha kuchipuka kwa biashara haramu (ukwepaji kulia ushuru na matumizi ya stampu bandia) hasa katika sehemu za magharibi ya Kenya.

Nyongeza ambayo haikutarajiwa ya asilimia 87 kwa gharama ya stampu za ushuru, iliyojulishwa kwetu mwezi Aprili 2017, pia imesababisha kupanda kwa gharama yetu ya biashara. Utekelezaji wa mifumo baguzi ya ushuru wa bidhaa na udumishaji baadhi ya masharti ya kibiashara yasiohusiana na ushuru, katika soko la EAC pia vingali changamoto kwa biashara yetu haswa tunapojaribu kupanua soko. Hata hivyo tunaendelea kushauriana na serikali husika kuondoa vizuizi hivyo vya biashara na wakati huo huo kuzingatia mkatamba wa kibiashara.

Ukuzi wa soko la pamoja la nchi za Mashariki na Kusini mwa Afrika (COMESA) hasa kuafikiwa kwa mikataba ya biashara huru, ungali lengo letu kuu. Kuondolewa kwa vizuizi vya biashara kutapanua soko na kutoa fursa ya ukuaji kwa biashara yetu haswa utengenezaji wa bidhaa.

Matokeo ya biashara

Mazingira yenye changamoto nyingi ambapo tunaendesha biashara yetu pia yanaathiri kasi ya ukuaji. Mapato halisi yalipungua kwa asilimia 6, kutokana na kufifia kwa soko la hapa nchini. Hata hivyo tulinakili faida kutokana na mauzo ya nje, ambapo tulishuhudia ukuaji kiasi.

Faida hiyo hata hivyo haingeweza kusawazisha upungufu ulionakiliwa katika soko la hapa nchini. Upungufu huo pamoja na nyongeza ya ghafla ya ushuru wa stampu, gharama kubwa ya kuratibisha upya shughuli zetu na nyongeza ya malipo ya riba, yalisababisha kupungua kwa asilimia 18 faida yetu kabla ya kulipa ushuru.

Mgao wa faida

Halmashauri ya Wakurugenzi inapendekeza mgao wa mwisho wa faida wa Shillingi 22.50 na kwa kila hisa kwa mwaka 2017, ambao utalipwa mnamo tarehe 11 mwezi wa Mei mwaka huu wa 2018 kwa wenye hisa watakaokuwa kwenye sajili kufikia tarehe 16 Machi 2018. Hii ni dhihirisho ya imani katika uendelevu wa biashara yetu.

Hii inaongeza mgao jumla wa mwaka 2017 hadi KSh. 26.00 kwa kila hisa (mwaka 2016: KSh. 43.00 kwa kila hisa).

Mabadiliko katika Bodi

Orodha ya wanachama wa sasa wa Bodi ya Kampuni inapatikana kwenye kurasa za 52 hadi 53.

Kwa niamba ya Bodi, ningependa kumshukuru katibu wa Kampuni Ruth Ngobi ambaye atastaafu baada ya mkutano mkuu wa kampuni, akiwa amehudumu kwa wadhifa huo kwa miaka 16. Atakayechukua mahali pa Ruth ni Mkuu wa Ushauri wa sheria, Waeni Ngea ambaye aliteuliwa kama katibu wa kampuni kuanzia siku ya 15 mwezi wa Februari, 2018 lakini ataanza kutekeleza rasmi majukumu yake siku ya 12 mwezi wa Mei 2018.

Matarajio

Ingawaje tunahisi kwamba changamoto za biashara tunakumbana nazo kwa wakati huu hazitamalizika hivi karibuni, nina uhakika kwamba Kampuni yetu ina ari, nia na uwezo kunakili matokeo mazuri zaidi katika siku zijazo. Bodi yangu ina imani katika mkakati wake, ambao msingi wake ni kutengeneza bidhaa za hali ya juu na nafuu, huku ikiendelea kuwekeza katika utoaji mafunzo kwa wafanyakazi wake ili kuimarisha utenda kazi wao.

Kwa niaba ya Bodi, ningependa kuwashukuru wafanyakazi, wawasilishaji bidhaa wetu, asasi za serikali na wadau wengine kwenye sekta hii, kwa juhudi zao katika kuhakikisha kwamba biashara yetu inanawiri. Nina imani kwamba tutaendelea kufanya kazi bega kwa bega, kuhakikisha kuwa tunanakili faida katika miaka ijayo kwa manufaa ya wenye hisa.

George Maina
Mwenyekiti

MANAGING DIRECTOR'S ***REVIEW***

> Despite various challenges in our operating environment, we registered some impressive wins; we grew market share in Kenya and recorded growth in our export volumes.

Beverley Spencer-Obatoyinbo Managing Director

A tough year

I am pleased to report that our Company successfully navigated a particularly challenging trading environment in Kenya and across our export markets to deliver a solid, albeit reduced set of results. My team and I are hard at work to reverse the lower performance and return the business to growth as Kenya's economy stabilises.

Adverse market conditions

In 2017, consumer affordability was adversely impacted by a slow-down in trading activity, high inflation and the prolonged election period in Kenya. Access to cash became a challenge for the consumer, who cut back on spending during the period.

Devaluation, drought and insecurity in our export markets, notably in the Democratic Republic of Congo, Somalia and Egypt, also reduced disposable income for consumers, leading to lower than expected growth.

Unpredictable and unstable regulatory and tax environment

As a business, we welcome balanced, evidence-based regulations to govern the way we operate. We also advocate for stable and predictable changes to the taxation environment as this amongst other things, enables us to plan better to remain competitive. This also supports the manufacturing pillar of the Government's Big Four agenda, and growth and development of over 80,000 people involved in our business.

Disproportionate increase in tax stamp costs

We continue to feel the effects of the 50% excise increase in December 2015, which led to unprecedented price increases for our affected products. The Excise Act of March 2017 introduced amongst other measures, a disproportionate and unjustifiable 87% increase in the cost of each tax stamp. This has added KSh. 161 million to the cost of doing business in Kenya, without clear benefit to the tobacco industry.

We continue to engage the Government to ensure a stable, predictable fiscal environment for the industry, as should be expected for a top four tax revenue generator.

The incidence of illicit trade, including products bearing counterfeit tax stamps, continues to increase to the detriment of legitimate trading companies and the Government. We continue to request government agencies to help enforce the laws and regulations against those trading in these products (as stated in the Big Four agenda).

Tobacco Control Regulations 2014

We continue our legal challenge against the Tobacco Control Regulations 2014 because we believe that substantial parts of these regulations are excessive and unconstitutional. We continue to engage government agencies to apply the current regulations in force to curb instances of inappropriate advertisements on display in our markets. This is critical to ensure there is a level playing field among all companies competing in the market.

Trade barriers

In 2017, we saw the introduction of discriminatory excise tax and maintenance of non-tariff barriers in the EAC in Uganda and Tanzania respectively.

We believe that these measures by some EAC countries threaten the effectiveness and potential benefits of the trade bloc and we therefore continue to actively engage the Community Secretariat and Partner State Representatives to promote trade and reverse these protectionist measures.

Business results

Despite these challenges, we registered some impressive wins. We grew market share in Kenya and saw exports to Somalia increase. Our underlying cost base remained competitive as we tried to offset the impacts of higher taxation and financing costs.

Gross and Net revenue declined 6% respectively, driven by a 7% decline in domestic volumes and lower mix, offset by a 4% increase in export revenues to USD 89 million (2016: USD 88 million) driven by stable volumes, incremental pricing, an improved mix with more sales coming from Somalia on the back of distribution expansion initiatives and slight foreign exchange gains.

Government revenue reduced by 6%, driven by lower excise collections because of the lower domestic volumes in the market.

Operating margin was down 2.2 percentage points, driven by the revenue decline, the 87% increase in the cost of tax stamps and inflationary operating cost increases offset by our productivity savings drive, which delivered over KSh. 750 million. Our intensive productivity drive through new working practices in operations and investments in technology has led to more efficient and effective ways of working. This has regrettably resulted in a reduction of 24 people from the BAT Kenya operations team. We have treated those affected by restructuring exercises with dignity, sensitivity and fairness.

Profit before tax declined by 18% because of lower operating profit, higher reorganisation costs and higher financing costs, due to lower profitability and working capital investment in the first half of 2017.

Winning in the market

During 2017, we continued to build for the future by rolling out consumer relevant innovative products into the market to drive growth in market share. We launched flavoured capsule products for Dunhill and Sportsman in Kenya and saw interest for the same in our export markets in Somalia and Mauritius.

To further build our trade partnerships in Kenya, we enhanced our support to our traders who felt the impact of lower disposable incomes by improving trading terms and driving a further increase in the number of stores that our distributors deliver to directly.

Our people

In 2017, we continued investing in our people by attracting the best in the market and by developing more high performing leaders who will inspire our teams to be more committed and engaged. We continue to drive a high performance culture by promoting coaching and continuous feedback. This will build a fulfilling, rewarding and responsible work environment.

I am proud to report that we have 15 Kenyans currently working in other markets who will be gaining invaluable experience they can capitalise on upon their return to Kenya.

Our efforts to develop our people were recognised through two awards:

- Top Employer Kenya and Africa 2018 certification by the Top Employers Institute, for excellence in employee conditions;
- Best Overall Employer of the Year 2017 by the Federation of Kenya Employers (FKE).

I am extremely proud and privileged to lead the BAT Kenya team and I am confident that together, we will deliver sustained growth into the future.

Confidence in our outlook

I believe we have the appropriate strategy and plans in place to return our business to growth into the future.

We will tap into the British American Tobacco Group's network and invest in innovative, high-quality products at an affordable price to our consumers. We will further enhance relationships with our trading partners who will avail these quality products to our consumers at their convenience and a competitive price. We will pursue growth opportunities in our region by striving for excellence in our factory's quality and cost competitiveness.

Efforts to return our business to growth will be enhanced by energised, collaborative and agile teams. We will build and invest in future leaders through more relevant training and development programmes both in and outside Kenya. We will modernise the work environment to complement this approach and ensure we have 'a great place to work'.

We will continue to engage the relevant government agencies to enhance stability and predictability in the industry. Specifically, we appeal to the Government to reconsider the unjustified increase in the cost of excise tax stamps, enable seamless trade across the EAC Member states and address the illicit trade challenge that threatens to erode legal business and Government revenues.

With these measures, I am confident that we are well placed to continue our success into the future.

Beverley Spencer-Obatoyinbo
Managing Director

TATHMINI YA MKURUGENZI MKUU

"Licha ya changamoto tulizokumbana nazo, tulipata ufanisi; soko letu hapa nchini lilipanuka, huku mauzo yetu katika nchi za nje yakiongezeka."

Beverley Spencer-Obatoyinbo Mkurugenzi mkuu

Mwaka mgumu

Ni furaha yangu kuwafahamisha kwamba kampuni yetu ilistahimili mazingira magumu ya biashara hapa nchini, na pia masoko yetu ya nje, na kupata faida, japo ilipungua. Hata hivyo nawahakikishia kuwa mimi pamoja na kikundi changu tutafanya kazi ya ziada kuhakikisha tunanakili ukuaji na kuongeza mapato kwa kampuni huku hali ya uchumi wa nchi ikizidi kuimarika.

Athari za hali ya soko

Katika mwaka wa 2017, uwezo wa wateja kununua bidhaa zetu uliathirika pakubwa kutokana na kufifia kwa shughuli za biashara, gharama ya juu ya maisha, pamoja na kipindi kirefu cha kampeni za uchaguzi hapa nchini. Upatikanaji pesa za matumizi ulikuwa changamoto, kwani watu wengi kutokana na kutotabirika kwa hali ya kisiasa baada ya uchaguzi walipunguza matumizi yao ya pesa.

Kupungua kwa thamani ya pesa, ukame na ukosefu wa usalama katika masoko yetu ya nje, hasa Jamhuri ya Kidemokrasia ya Congo (DRC), Somalia na Misri, pia viliathiri biashara yetu, hali iliyoyumbisha kiwango cha ukuaji.

Mifumo isiyobashirika ya uthibiti na ushuru

Kama biashara, tunaunga mkono mifumo inayozingatia uwazi na haki ya uthibiti. Pia tunahimiza uzingatiaji mifumo inayoweza kutabirika ya utozaji ushuru, ili baadhi ya mambo mengine, tuweze kupanga vyema shughuli zetu, hasa ya kifedha kuambatana na mifumo hiyo. Hatua hii pia inaunga mkono jitihada za serikali za kuimarisha sekta ya utengenezaji bidhaa (mojawapo ya agenda kuu nne za serikali) na kuinua kimaisha zaidi ya watu 80,000 wanalio katika biashara hii.

Ongezeko kubwa la gharama ya stampu za ushuru

Tunaendelea kuhisi athari za nyongeza ya aslimia 50 ya Ushuru wa sigara, iliyotekelezwa mwezi Disemba mwaka wa 2015, na kusababisha kuongezeka kwa bei ya bidhaa kwa kiwango kikubwa. Sheria za ushuru wa bidhaa za mwezi wa Mechi 2017, ilichangia nyongeza ya asili mia 87 ya gharama ya stampu ya ushuru. Ushuru huo usiokuwa na manufaa bayana kwa sekta ya tumbaku hapa nchini, umeongeza hadi shilling million 161 gharama ya kufanya biashara hapa nchini.

Tunaendelea kujadiliana na serikali ili kuhakikisha sekta yetu ina mazingira bora ya kibiashara, ili kutuwezesha kubashiri matokeo ya biashara yetu, kama inavyotazamiwa shirika ambalo ni miongoni mwa mashirika manne yanayochangia ushuru kwa wingi.

Visa vya biashara haramu, ikiwemo bidhaa zilizo na stampu ghushi za ushuru pia vinaendelea kuongezeka hapa nchini na kuathiri vibaya mapato kwa biashara halali na pia kwa serikali. Tunaendelea kuisihi serikali, kupitia idara zake mbali mbali, itekeleze sheria ili kuthibiti hali hii (kama ilivyo panga katika agenda nne kuu za serikali).

Kanuni za Uthibiti wa Tumbaku 2014

Tunadumisha pingamizi zetu za kisheria dhidi ya Kanuni za Uthibiti wa Tumbaku 2014, kwa sababu tunaamini kuwa ni adhibifu na zinakinzana na katiba.

Hata hivyo tutaendelea kuhimiza taasisi husika za serikali kutekeleza masharti yalioko kwa sasa kukabiliana na matangazo ya biashara yanayokiuka maadili ya kibiashara. Hii ni muhimu kwa sababu itahakikisha kuna usawa wa kibiashara miongoni mwa kampuni kwenye sekta ya tumbaku.

Vizuizi vya biashara

Katika mwaka wa 2017, tumeshuhudia uanzishaji wa mfumo baguzi wa ushuru wa bidhaa, na udumishaji vizuizi vya biashara visivyohusiana na ushuru nchini Uganda na Tanzania.

Tunaamini vizuizi hivyo vinavyotekelezwa miongoni mwa baadhi ya mataifa yanachama ya jumuiya ya Afrika Mashariki-EAC ni tisho kwa ufanisi na manufaa ya muungano wa biashara wa jumuiya hiyo, na ndiyo sababu tutaendelea kujadiliana na makao makuu ya Jumuiya hiyo kwa lengo la kuafiki makubaliano yatakayosaidia kubadili vizuizi hivyo.

Matokeo ya biashara

Licha ya changamoto tulikumbana nazo katika kipindi hicho, twaweza kusema kwamba tulipata ufanisi. Mgao wetu wa tumbaku, hapa nchini lilipanuka, huku mauzo yetu katika nchi ya Somalia yakiongezeka. Gharama yetu ya matumizi pia iliongezeka kiasi, huku tukijaribu kukabiliana na athari za viwango vya juu vya ushuru, na gharama ya kufadhili shughuli zetu.

Mapato jumla na halisi yalipungua kwa asilimia 6, kutokana na upungufu wa asilimia 7 katika mauzo yetu ya hapa nchini, ongezeko la asilimia 4 katika gharama ya mauzo ya nje hadi dola za Marekani milioni 89 (2016: milioni 88), kutokana na mauzo bora nyongeza ya bei hasa nchini Somalia ufunguzi wa vituo zaidi vya kuuza bidhaa zetu yaliimarika na kuchangia kuongezeka kiasi kwa pato la biashara ya kigeni.

Ushuru kwa serikali nao ulipungua kwa asilimia 6 kutokana na kufifia kwa ukusanyaji ushuru wa bidhaa kulikosababishwa na kupungua kwa mauzo katika soko la hapa nchini.

Mapato ya kampuni baada ya kulipia huduma nyingine msingi yalipungua kwa asilimia 2.2 kutokana na kupungua kwa mapato jumla, ongezeko la ushuru wa stampu la asilimia 87, gharama ya juu ya utekelezaji shughuli zetu, ambayo hata hivyo ilifidiwa na akiba ya shilling zaidi ya milioni 750 zilizookolewa kupitia jitihada zetu za kupunguza matumizi. Kadhalika utendaji wetu umeimarika pakubwa kutokana na uzinduzi wa kanuni mpya za utenda kazi, na uwekezaji katika teknolojia ya kisasa. Hata hivyo mabadiliko hayo yamesababishwa kuondolewa kwa watu 24 kwenye kikundi cha BAT Kenya. Kuondolewa kwa wafanyakazi hao hata hivyo kulitekelezwa kwa uangilifu mkubwa na heshima.

Faida kabla ya kulipa ushuru ilipungua kwa asilimia 18 kwa sababu ya faida ndogo ya matumizi, gharama kubwa ya kutekeleza marekebisho, gharama ya kufadhili shughuli zetu, na kupungua kwa mtaji wetu katika nusu ya kwanza ya mwaka 2017.

Kunawiri katika soko

Wakati wa kipindi cha mwaka 2017, tuliendelea kuweka msingi thabiti wa siku za usoni kwa kuzindua bidhaa mpya ili kuongeza hata zaidi upeo wetu katika soko. Tulizindua aina mpya ya chapa ya Dunhill na Sportsman huku mahitaji ya sigara aina hii yakiripotiwa kuongezeka katika nchi za Somalia na Mauritius.

Tuliboresha ubia wetu wa kibiashara hapa nchini, kwa kuwasaidia wauzaji bidhaa zetu, walioathirika kutokana na kufifia kwa biashara, kwa kuboresha kanuni za biashara, kando na kufungua vituo zaidi vya kuuza bidhaa zetu, ili kuwafikia kwa urahisi wateja wetu.

Watu wetu

Katika mwaka wa 2017, tuliendelea kuboresha mazingira ya kufanya kazi, ili kuwavutia wafanyakazi walio na ujuzi, na ambao watawapa msukumo wafanyakazi wengine kwa minajili ya matokeo bora. Tunaendelea kuhimiza mtindo wa kufanya kazi kwa bidii, kupitia utoaji ushauri na upokeaji maoni. Hii inasaidia katika kubuni mazingira bora ya kufanya kazi.

Nina furaha kuwafahamisha kwamba kuna Wakenya 15, ambao kwa wakati huu wanafanya kazi katika masoko mengine na ambao wanapata uzoevu wa kazi utakaosaidia kampuni yetu watakapo rudi nchini.

Juhudi zetu za kuwapa uwezo watu wetu zimetambulika kupitia matuzo mawili:

- Cheti cha Mwajiri Bora Kenya na Africa mwaka 2018, kutoka kwa Taasisi ya Waajiri Bora, kutokana na juhudi za kujali maslahi ya wafanyakazi.
- Mwajiri bora Kenya wa mwaka 2017 kutoka kwa Shirikisho la Waajiri la Kenya.

Ni fahari na furaha yangu kuongoza kampuni ya BAT Kenya, na nina uhakika kwamba kwa pamoja tutaiwezesha kampuni hii kunakili ukuaji mkubwa kibiashara.

Matarajio yetu

Kuambatana na mtazamo wa bodi yetu, naamini tuna mkakati kabambe na mipango mwafaka ya kurejesha biashara yetu katika mkondo wa ukuaji, sasa na siku zijazo.

Tutatumia fursa ya mtandao mkubwa wa kampuni ya kundi la British American Tobacco, kuwekeza katika ubunifu, na kutengeneza bidhaa za ubora wa hali ya juu, lakini nafuu kwa wateja wetu. Pia tutaimarisha ushirikiano na washirika wetu kibiashara, ambao tunawategemea kusambaza bidhaa zetu, kwa wakati ufaao na kwa bei inayofaa. Pia tutatumia fursa za biashara zilizopo katika kanda hii, kupanua biashara yetu na kuboresha viwanda vyetu kwa manufaa ya wenye hisa.

Kurejea kwa biashara yetu katika ukuaji wa haraka hata hivyo kutategemea kikundi cha wafanyakazi kakamavu, kinachoshirikiana na kibunifu. Tutajizatiti kuimarisha ujuzi wa wafanyakazi wetu, kupitia mafunzo ya ziada hapa nchini na pia nje ili kuimarisha mazingira bora ya kazi.

Tunaendelea kujadiliana na idara mbali mbali za serikali ili kuboresha mazingira ya biashara yetu na kuwa thabiti. Tutaiomba serikali kutuondelea ushuru wa juu na kuimarisha biashara katika wanachama wa mataifa ya EAC na wakati huo huo kukabiliana na changamoto za biashara haramu inayo athiri vibaya bishara yetu halali na kuinyima serikali ushuru.

Kwa hatua hizi, nina hakika kwamba tuna uwezo wa kunakili ufanisi wa biashara yetu hata zaidi katika siku za usoni.

Beverley Spencer-Obatoyinbo
Mkurugenzi mkuu

FINANCE DIRECTOR'S ***OVERVIEW***

"Despite our best efforts, the challenging trading environment led to a reduction in profit before tax."

Sidney Wafula Finance Director

Financials under pressure

Despite our best efforts, the challenging trading environment led to a reduction in profit before tax. Trends on key performance measures are noted below:

Income statement

Revenue

Net revenue was under pressure, declining by 6% to KSh. 18,673 million, driven by the 7% volume decline and lower mix in the domestic market as reported in the Managing Director's review. Domestic revenues were down 14% to KSh. 9,518 million while export revenues grew by 4% to KSh. 9,155 million, driven by distribution expansion and pricing in Somalia and marginal inflationary pricing in our contract manufacture markets mainly the Democratic Republic of Congo (DRC), Mauritius and Uganda.

Operating profit

Operating profit declined by 12%. This was driven by the revenue decline mentioned above, an unexpected 87% increase in cost of tax stamps which increased operating costs by KSh. 161 million in 2017 and inflationary cost increases partially offset with productivity savings of over KSh. 750 million.

Operating margin

Operating margin (profit from operations as a percentage of net revenue) fell by 2.2 percentage points. The lower domestic volume and mix, minimal pricing benefits in the domestic market (due to affordability changes) and the unplanned regulatory costs drove the decline.

Gross revenue (KSh.)
34.5bn

Contribution to Government taxes (KSh.)
18.0bn

Operating margin
30.8%

Profit before tax (KSh.)
4.9bn

Dividend per share (KSh.)
26.00
per share

Profit before tax

Profit before tax declined by 18%, driven by the decline in operating profit together with higher reorganisation costs from redundancies and higher net finance costs, due to the lower profitability and the higher working capital investment in the first half of 2017 to ensure continuity of supply.

Tax

The effective corporate tax rate was 31.5% (2016: 28.4%). This was driven by one-off gains from property disposals in 2016 taxed at a lower rate, higher depreciation on revaluation in 2017 and a prior year deferred tax adjustment for permanent differences on land and buildings.

Major taxes included in our financial statements are as shown below:

	2017	2016
	KSh.'mns	KSh.'mns
Tobacco Excise	12,290	12,961
Value Added Tax	3,504	3,865
Corporation tax	1,509	1,760
Pay As You Earn	725	642
Total	18,028	19,228

Dividends

This year, the Company will pay dividends of 78% of earnings, calculated with reference to the diluted earnings per share. With the recommended final dividend of KSh. 22.50 per share, the total dividends per share for 2017 are KSh. 26.00 per share, compared to KSh. 43.00 per share in 2016.

Cash flow

Cash generated from operations reduced by 20% to KSh. 6,419 million, reflecting the reduced profitability and higher working capital investment in the first half of 2017. However, this has been offset by significant efforts to optimise inventory holdings to free up cash.

Alternative cash flow

The IFRS cash flow includes all transactions affecting cash and cash equivalents, including financing. The alternative cash flow included here is presented to illustrate the cash flows before transactions relating to borrowings. The conversion of operating profit to cash generated from operations remains strong.

	2017	2016
	KSh.'mns	KSh.'mns
Operating profit	5,361	6,206
Depreciation and amortization	781	760
Profit from operations before depreciation and impairment	6,142	6,966
Decrease in working capital	284	1,031
Net capital expenditure	(379)	(286)
Operating cash flow	6,047	7,711
Net interest paid	(494)	(315)
Tax paid	(1,216)	(2,510)
Cash generated from operations	4,337	4,886
Operating cash flow conversion	113%	124%

Other matters

Accounting standards and policies

BAT Kenya has prepared its annual Consolidated Financial Statements in accordance with IFRS. The application of the accounting standards and the accounting policies adopted by BAT Kenya are set out in the Group Manual of Accounting Policies and Procedures (GMAPP).

There were no material changes to the accounting standards or policies applied in 2017 from those applied in 2016. Future changes applicable on the accounting standards that will be applied by the Group are set out in the Notes on the Financial Statements (note 1 – Accounting Policies). The impact is not expected to be material to the Group's results.

Sidney Wafula
Finance Director


A winning portfolio of global & local brands
We consistently strive to offer the highest quality and most innovative product range to satisfy the different needs of our consumers.

DELIVERING VALUE THROUGH INNOVATION

18 AND ABOVE ONLY

Sale of tobacco products to any person under the age of eighteen (18) is prohibited by law

WARNING: SMOKING HARMS PEOPLE NEXT TO YOU

ONYO: UVUTAJI WA SIGARA HUDHURU WATU WALIO KARIBU NAWE

OUR STRATEGIC FRAMEWORK
TRANSFORMING TOBACCO

Our strategy remains as relevant today to drive our transforming tobacco ambition as it was when it was first rolled out. It enables us to deliver growth today while driving the investment required to deliver our transformational agenda.

Our vision remains clear: while combustible tobacco products will remain at the core of our business for some time to come, we understand that long-term sustainability will be delivered by our transforming tobacco ambition.

Our vision

World's best at satisfying consumer moments in tobacco and beyond.

Our consumers are at the core of everything we do and our success depends on addressing their preferences, concerns and behaviours.

We know that these are fragmenting and evolving at an unprecedented pace, and consequently, we are clear that to win in this space we need to understand our consumers' preferences and further invest in a pipeline of ever evolving innovations.

Our mission

Delivering our commitments to society, while championing informed consumer choice.

We have long known that, as part of a major international business, we have a responsibility to address societal issues with our tobacco products, and that, as our business continues to grow, so does our influence and the responsibility that comes with it.

We are also clear that we have a duty to our shareholders to ensure we continue to deliver today and invest for a sustainable future and to our consumers to provide high quality tobacco products.

Our transforming tobacco ambition, with its core objective of providing consumers with more choice and more innovation will allow us to: satisfy these consumers; address societal concerns at large and provide a sustainable, profitable future for our shareholders.

Strategic focus areas

Our four key focus areas remain fundamental to our strategy as we focus on our transforming tobacco ambition.

Growth

Developing our portfolio while continuing to drive revenue growth from our traditional combustible products.

Productivity

Effectively deploying resources and managing our cost base to release funds for investment.

Winning organisation

Ensuring we have great people with the right skill sets in the right teams to drive the transformation of our business.

Sustainability

Ensuring a sustainable business that meets the expectations of all our various stakeholders.

Guiding principles

Our guiding principles provide clarity about what we stand for. They form the core of our culture and guide how we deliver our strategy.

Enterprising spirit

We value enterprise from all of our employees, giving us a great breadth of ideas and viewpoints to enhance the way we do business.

We have the confidence to passionately pursue growth and new opportunities while accepting the considered entrepreneurial risk that comes with it.

We are bold and strive to overcome challenges. This is the cornerstone of our success.

Freedom through responsibility

We give our people the freedom to operate in their environment, providing them with the benefits of BAT Group' scale but also the ability to succeed locally.

We always strive to do the right thing, exercising our responsibility to society and other stakeholders.

We use our freedom to take decisions and act in the best interest of consumers.

Open minded

Our corporate culture is a great strength of the business and one of the reasons we have been, and will continue to be, successful.

We are forward-looking and anticipate consumer preferences, winning with innovative, high quality products.

We listen to, and genuinely consider, other perspectives and changing social expectations. We are open to new ways of doing things.

Strength from diversity

Our employee population comprises people from over ten nations, giving us unique insights into local markets and enhancing our ability to compete across different markets.

We respect and celebrate each other's differences and enjoy working together.

We harness diversity – of our people, cultures, viewpoints, brands, markets and ideas – to strengthen our business. We value what makes each of us unique.

OUR BUSINESS **MODEL**

At the center of our business is the manufacture and marketing of superior combustible tobacco products, for more than a century.

Our sustainable approach to sourcing, production, distribution and marketing helps us to create value for a wide group of stakeholders from farmers to consumers.

We use our unique strengths and employ our resources and relationships to deliver sustainable growth in earnings for our shareholders.

Our people and relationships

We employ over 400 permanent employees, with a workforce that is diverse and multi-cultural.

The quality of our people is a major reason for our continued solid performance.

In return, we commit to investing in our people as we do in our brands.

We encourage a culture of personal ownership and value our employees' talents and abilities. Their diverse perspectives help us succeed.

We also have excellent relationships with a range of stakeholders, including farmers, retailers and distributors.

We engage with the relevant regulators to support regulation that is based on robust evidence and thorough research, that respects legal rights and livelihoods and delivers on the intended policy aims while recognising unintended consequences.

Source

What we do

While the Company does not own tobacco farms or directly employ farmers, we contract over 5,000 farmers to produce high quality tobacco leaf for our tobacco products.

What makes us different

- We provide on-the-ground support and advice for our contracted farmers to help ensure consistency and quality of tobacco leaf.
- We facilitate crop insurance, health insurance and provide interest free loans in form of farm inputs to further support our farmers.
- We use global best practices to ensure we work with reliable, efficient and responsible farmers.

Market

What we do

We offer adult consumers a range of high quality cigarettes. Our portfolio covers all segments, from value-for-money to premium.

What makes us different

- Our successful portfolio of global and local cigarette brands continues to deliver significant value over the long term and meet a broad array of adult consumer preferences, based on sound consumer insights.

Produce

What we do

We manufacture high quality products in our manufacturing hub which comprises a cigarette factory in Nairobi and a green leaf threshing plant (GLT) in Thika. We also ensure that these products and the tobacco leaf we purchase are in the right place at the right time. We work to ensure that our costs are globally competitive and that we use our resources as efficiently as possible.

What makes us different

- The Kenya manufacturing hub is one of the three strategic factories in Africa, for the BAT Group. Its strategic location enables us to maximise efficiency and ensure that products for both the domestic and export markets are where they need to be at the right time.
- Our production facilities are designed to meet the needs of an agile and flexible supply chain and provide a world-class operational base that is fit for the future.

Consumers

We place consumers at the centre of our business, we invest in world-class research to understand changing consumer preferences and buying behaviour. This drives our leaf sourcing, product development, innovation, brands and trade activities.

We aim to satisfy consumers with a range of inspiring products and address expectations about how we should market them.

Distribute

What we do

We distribute our products effectively and efficiently using distribution models suited to the respective circumstances and conditions. Most of our cigarette volume is sold by retailers, supplied through our distributors. We continuously review the route to market for our products, including our relationships with wholesalers, distributors and logistics providers.

What makes us different

- Our relationships with, and efficient distribution to, retailers countrywide ensures we can offer the products our adult consumers wish to buy, where and when they want them.
- Our distribution capability enables new product innovations to be distributed to markets quickly and efficiently.

Resources for success

Innovation

We make significant investments to deliver innovations such as capsule products, that satisfy or anticipate consumer preferences and generate growth for the business across all categories.

World Class Science

As part of the BAT Group, we benefit from scientific research programmes in a broad spectrum of scientific fields including molecular biology, toxicology and chemistry.

The BAT Group is transparent about its science and publishes details of its research programmes on its dedicated website www.bat-science.com and the results of its studies in peer-reviewed journals.

BUSINESS REVIEW

A LEADERSHIP PORTFOLIO THAT ACCELERATES GROWTH

Product development and innovation

Through a portfolio of leading global and local brands, we consistently strive to offer the highest quality and most innovative product range to satisfy the different needs of our consumers. The ability to deliver this objective comes from a deep understanding of the Kenyan consumer, which is the result of a long history of interaction between our customers and brands and consistent research programmes using the latest tools to gather pertinent consumer and market insights.

During 2017, we carried out an ambitious piece of research - Product Space Mapping - to deepen our understanding of consumer preferences and emerging trends in tobacco taste as well as to benchmark our products against competitive offers. This research confirmed the strength of our products and gave indications for innovation opportunities.

We continued to invest in innovation across our brand portfolio. Dunhill was once again, the innovation leader in Kenya following our launch of the first Double Capsule product in the market. Within less than a year in market, Dunhill Double Capsule already accounts for 25% of the Dunhill Family volume contribution.

Innovation was not limited to the premium segment. Sportsman offered new and innovative products within the value for money segments, with the launch of Sportsman Switch and Sportsman Full Flow during the second half of 2017. Since introducing these new product lines into market, Sportsman has achieved high levels of distribution in a very short period and generated positive consumer reactions.

Going forward, we will continue to focus on quality and innovation to generate value for the consumer and sustain consumer preference for BAT brands.

INNOVATIVE ROUTE TO MARKET INITIATIVES AND PARTNERSHIPS

A member of the BAT Kenya field force engages with one of our trade partners.

To complement the improvements made to our product portfolio, we continued to improve the quality of our distribution and trade partnerships to best meet our customer and consumer needs. Through collaboration with our distribution partners, we conducted and embedded the transformative 'Everyday Coaching' and 'POSITIVE' programmes to refine the field teams' leadership and business management capabilities. Through our recognition programme, 'Bingwa', (Swahili for Champions), six of our team members were rewarded with a trip to South Africa, for a business best practice transfer experience, for their exemplary performance within the year.

In 2017 marked the first-year anniversary of 'Faida Max', our flagship wholesaler programme that is growing more than 600 of our traders' businesses through a 'pay for performance' model. Our wholesalers can increase their earnings by delivering superior market performance, and as a value add, they can also access business enablers such as credit and insurance facilities. Into 2018, we plan to partner with more than 1,000 traders on this programme.

Our innovative approach to business enables us to directly and indirectly partner with more than 59,000 retailers across the country. In 2017, we launched another 'pay for performance' retailer programme, 'Jenga Bizna'. The programme aims to bring our partners along with us on our growth journey, which illustrates our commitment to building sustainable partnerships. 'Jenga Bizna' runs on cutting edge technology that enables the retailers to track their performance, and adjust their business management behaviour to deliver on our joint business objectives.

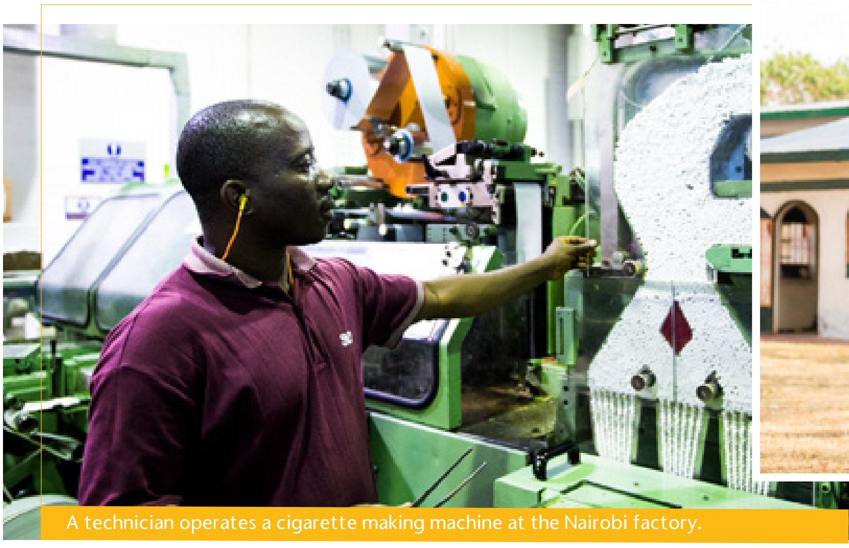
Our business practices continue to evolve to keep ahead of the trends that are redefining our business landscape. One such area is cashless transactions, which are now well entrenched in the Kenyan economy.

To reduce risk and improve ours and our business partners' bottomline, we have continued to scale up cashless platforms to every level of our distribution chain. As a result, various benefits have accrued to our business partners, including selling time optimisation and access to credit for traders. A key example is our partnership with Safaricom, where the 'M-Pesa Kadogo' platform has enabled consumer purchases at points of sale across the country using mobile money.

A group of trade partners on a capacity building trip to South Africa.

A team of trade partners are presented with a pick-up car, which they won during the Faida Max one year anniversary celebrations in 2017.

OUR PRODUCTIVITY AGENDA



A technician operates a cigarette making machine at the Nairobi factory.

A contracted farmer shows his upgraded house to a BAT Kenya field extension officer.

World-class manufacturing capabilities

Our strategy to embed 'Integrated Works Systems' (IWS) in our operations is working well and delivering sustainable benefits to the business. IWS is a structured approach that was introduced in 2015 to consistently produce superior quality products, improve factory efficiencies, increase productivity, deliver savings and eliminate waste.

At our Kenya manufacturing hub, 64% of our machinery is now on IWS and subsequently, we have activated six critical pillars (Leadership, Organisation, Autonomous Maintenance, Progressive Maintenance, Focused Improvement and Quality). Our goal to achieve 100% employee involvement and a no loss culture is taking root in Operations and enabling improvements in performance.

Our efficiencies have improved by an average of 11% in 2017 versus 2016. The improved efficiencies have enabled our supply chain measure of delivering from our factory on time and in full (OTIF) to improve significantly by 4% to a world class level of 98%. We will continue to use IWS to make the most of our existing machinery. The improved performance above has led to a capital expenditure avoidance of over KSh.100 million.

The focused improvement approach has delivered 20% reduction in customer complaints in 2017 versus 2016 leading to world class service levels to our customers scoring a rating of 99%.

Our focus on loss elimination has driven improvements in financial metrics with manufacturing cost per unit registering a reduction of 10% and leaf waste reducing by 2.4% versus 2016.

Energy management programmes

Our investments in energy conservation continue to deliver savings and win accolades. In 2017, the Kenya Association of Manufacturers (KAM) recognised BAT Kenya as the Company with the Best Energy Committee and as the Best Fuel Saving Company.

Our investment in energy saving projects, coupled with improved efficiencies, has seen our total energy utilisation consumption per unit of production reduce by 7.5% in 2017 versus 2016 and the energy assessment score improve by 4%.

We continue to implement initiatives to reduce water consumption through water reticulation projects, sub-metering, use of sensors and currently, we are commissioning an effluent treatment system to boost water-recycling. These projects have seen our water usage per unit production reduced by 22% over the last 12 months.

Our waste recycling rate improved from 95% in 2016 to 100% in 2017, thus ensuring no waste was added to landfill sites. All solid waste generated at the factory is sold off for recycling and the proceeds are used to manage the costs of running the waste management plant.

Health and safety

The safety of our employees and contractors is our top-most priority. We continue to enhance our safety culture through our Incident Elimination (IE) Daily Management System. In November 2017, we celebrated a remarkable milestone, achieving 5 years with Zero Lost Time Injury (LTI).

> "Congratulations to the Nairobi team for this fantastic achievement. This is a significant milestone which only comes from continuously improving the EH&S culture throughout the organisation and places Kenya amongst the top performing factories within BAT Group. Well done!"

Paul Oakley
BAT Global Head of EHS

Enhancing farmer livelihoods

As an international business, we play an important role in the communities in which we operate. Beyond our corporate social investment initiatives across Kenya, we have programmes that ensure the long-term sustainability of our tobacco leaf supply chain and enhance farmer livelihoods in the communities we operate.

In 2017, we continued our partnership with over 5000 farmers who are mainly concentrated in Migori, Bungoma and Meru counties. Our long and proud history of building sustainable relationships with farmers has yielded mutual benefit; farmers receive the resources and support they need to be successful whilst our business secures a long-term supply of high quality tobacco leaf which ensures the integrity and quality of our products to satisfy our consumers.

We continued to facilitate crop insurance for our farmers and in 2017, this insurance scheme paid out KSh. 79.5 million to farmers who suffered crop losses due to various reasons, including effects of the prolonged drought that is still being felt in parts of the country.

Despite the harsh weather conditions, our partnership with our contracted tobacco farmers yielded 7 million kilograms of tobacco, earning them total net payment of KSh. 831 million. Alongside these earnings, farmers were also issued 8,800 kilograms of certified maize seeds for food crop production which is part of our Sustainable Agriculture Programme "THRIVE".

The farmers' Savings and Credit Cooperative Societies (SACCOs) introduced in 2016 continued to provide economic empowerment to our farmers. These SACCOs are now performing services that generate additional income for our farmers.

Going forward, we shall continue to refocus leaf operations in areas with a more reliable weather patterns and potential for future expansion to deliver quality and productivity.

ENERGISED, COLLABORATIVE AND AGILE TEAMS

Accolades received in 2017 for HR Excellence

Our Strategic Leadership Agenda: *#deliverasone2022*

BAT Kenya ensures employees are directly involved and engaged in delivering business results. In 2017, the Leadership Team shared with all employees the Strategic Leadership Agenda (SLA) for the next five years. Our SLA, 'deliver as one 2022', seeks to transform the organisation to achieve exceptional business results, whilst inspiring and providing a great place to work for our employees.

The business ambition was revealed during an informal afternoon at our Likoni Road office, where employees were taken through how each individual's contribution to this ambition is critical to its achievement.

deliver as One KENYA 2022

Organisational Excellence: Global certification and local recognition

Although our business is complex and competitive, it has always been guided by the highest standards of excellence. Our reputation for high quality and innovative tobacco products is the result of our commitment to recruiting, developing and retaining outstanding employees and building a great place to work.

BAT Kenya was certified Top Employer in Kenya and Africa 2018 by the Top Employers Institute. We were also named Kenya's Overall Best Employer of the Year by the Federation of Kenya Employers.

"This is a significant milestone for the HR team who work tirelessly to facilitate talent development, building a great cultural environment and therefore leaving a legacy of leaders for our business; a key pillar of BAT's success."

Beverley Spencer-Obatoyinbo,
Managing Director, BAT Kenya

top EMPLOYER KENYA 2018
CERTIFIED EXCELLENCE IN EMPLOYEE CONDITIONS

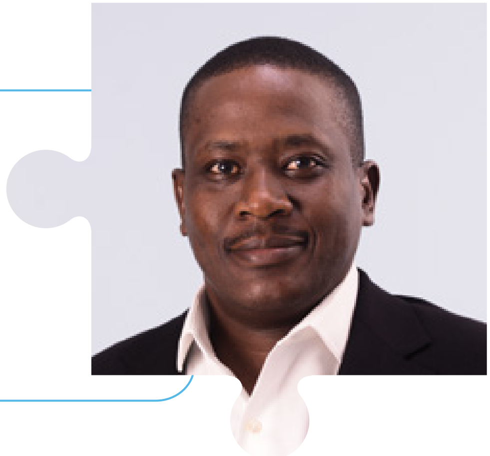
top EMPLOYER AFRICA 2018
CERTIFIED EXCELLENCE IN EMPLOYEE CONDITIONS

Building a legacy of leaders

BAT Kenya is a proud exporter of talent within the BAT Group, with 15 employees currently on assignment in Asia-Pacific, Europe and across Africa. Investing in our key talent remains a priority and enables us to provide a superior employee value proposition, whilst at the same time ensuring a solid talent pipeline for the future.

"I am currently on my second assignment based in Hong Kong as Head of Regional Regulatory Engagement for Asia Pacific & Middle East Region. Prior to this, I worked in London as Senior Legal Counsel for the Western Europe region. My journey so far has been enriching and insightful, working on global projects that have given me the opportunity to experience different cultures first-hand, develop a broader world-view and build capabilities at a global level."

Connie Anyika
Head of Regional Regulatory Engagement for BAT Asia Pacific & Middle East Region



"Over the last 17+ years, I have benefited from excellent coaching & mentoring from the senior leaders in BAT. This has prepared me for an international career that has been both stretching & rewarding; it's taken me from Kenya to South Africa and currently in-charge of Operations for West Africa, based in Nigeria. I can only describe my experience as AMAZING!"

Charles Kyalo
Head of Operations, BAT West Africa Area

BAT Kenya provides an impactful leadership training programme to young graduates through the Global Graduate Programme.

The programme is designed to equip young graduates with solid functional and leadership capabilities to enable them to take on first level managerial roles after 12 months.

In 2017, five young Kenyans graduated from the Programme, of which two are now on international assignments outside of Kenya. The Global Graduate Programme includes a two-week global leadership workshop where participants get to interact with peers from around the world as well as engage with senior leaders in the Group.

Graduates of the BAT Global Graduate Programme 2017 meet with BAT Group CEO Nicandro Durante (third from left) at BAT's head office in London.

Long Service Awards 2017

Re-affirming our commitment to our Diversity Agenda

A great place to work

Our people strategy is underpinned by our Guiding Principles, which provide certainty about what we stand for and act as a compass to guide our behaviour. These include: *strength from diversity, open minded, enterprising spirit and freedom through responsibility.*
On the back of our continuous efforts to live these guiding principles, BAT Kenya posted impressive performance scoring 82% in the BAT Group's 2017 Sustainable Employee Engagement Index (measured through the BAT Groups' Employee Opinion Survey – 'Your Voice').

Sustainable employee engagement is the intensity of employees' connection to the organisation and is marked by committed efforts to achieve business goals in an environment that supports productivity and personal well-being.

In addition, our diversity agenda goes a long way to drive sustainable employee engagement. For us, diversity means embracing the differences brought about by a rich mix of employees of different nationalities, gender, generation with professional experience and skills.

To this end, BAT Kenya today has 24% of its employee population as women in managerial positions, including the role of Managing Director, whilst employees with over 15 years of service account for 20% of the population.

OUR SUSTAINABLE APPROACH

Our socio-economic contribution

Our operations in Kenya span over 100 years. Throughout this period, we have consistently invested in our business and contributed to socio-economic development in the country.

BAT Kenya generates direct and indirect employment and business opportunities for more than 80,000 Kenyans in tobacco farming and processing, cigarette manufacturing, tobacco product distribution, urban and rural retailing, wholesale trade, transport, logistics and domestic procurement amongst others. This has further benefited thousands of people in the communities where we operate.

Our year on year investments and tax remittances to the Exchequer have further contributed to the Country's economic growth. Over the past five years, we have invested more than KSh. 10.3 billion in tobacco farming, leaf processing and our cigarette manufacturing factory in Nairobi and have paid over KSh. 80 billion to the Exchequer in form of various taxes over the last four years.

We are also a leading exporter in Kenya, making us a significant foreign currency earner for the country. In 2015, we were recognised as a Top Exporter by the Kenya Revenue Authority.

We protect the environment in which we operate

Reducing the environmental impacts of what we do is a key priority for us and as such, we work with local communities and relevant authorities to address impacts from our business activities as well as environmental pressures caused by the evolution of our ecosystems such as climate change and impact of human activity.

Our environment conservation initiatives help farmers to preserve natural forests through afforestation programmes that replenish depleted resources and develop new ones where they are needed. In 2017, we planted 1.7 million trees across the country in partnership with tobacco farmers and tree farmers and county governments. Some of our ongoing projects include the rehabilitation of 42-hectares in Ag'ongo hills where we have planted 300,000 tree seedlings of assorted species in partnership with the county government of Migori. We also participate in national and global environment preservation initiatives. Initiatives such as planting 1500 tree seedlings in conjunction with NEMA at Kijabe hospital to mark the 2017 World Environment Day.

On the biodiversity front, we have partnered on a bagasse briquetting project with South Nyanza Sugar Company Limited (Sony Sugar) to provide alternative fuel for tobacco curing. Currently, the briquetting plant has a capacity to produce briquettes to cure up to 40% of the tobacco we will grow in the next five years thus saving millions of trees.

A tree for every Kenyan:

To date, we have recorded over 50 million surviving trees planted in partnership with our farmers since 1978.

We partner with various county governments and relevant national authorities in environmental conservation initiatives.

Biodiversity: A farmer holds a briquette used for curing tobacco

Our approach to regulation

In 2017, the regulatory environment in Kenya continued to be challenging. In December 2014, the Cabinet Secretary for Health gazetted the Tobacco Control Regulations 2014 (TCR 2014) intended to guide the implementation of the Tobacco Control Act, 2007.

BAT Kenya filed a legal challange against some of the provisions of the TCR 2014, including the introduction of the *solatium compensatory contribution*, extension on public place smoking and limitations on industry and government interaction. We contested the legality of the TCR 2014 on a number of grounds including breaches of the Constitution and failure of the Ministry of Health to release the required technical information for the implementation of the TCR 2014 in time. We await the hearing of this matter.

BAT Kenya is not opposed to regulation. We support regulation that is balanced, evidence based and actually helping to achieve the intended public health objectives. Regulation that does not meet these criteria, could have unintended consequences such as stimulating illicit trade and harassment of members of the public and traders. We therefore will continue to seek opportunities to contribute to the debate and work with the regulators to address industry issues.

Working with Counties

The devolved system of Government, continues to evolve. This system presented some challenges for the business as some counties developed proposals to introduce new business levies and regulations, which are bound to add cost and complexity to our business.

To address these challenges, we engaged our stakeholders to highlight the potential impact of this approach on the sustainability of our operations.

In 2017, we facilitated a variety of training sessions with our Trade Marketing and Distribution teams across the country to enable them to engage appropriately with various stakeholders. We continue to develop opportunities to strengthen existing partnerships with county stakeholders, develop new ones and work together to ensure a conducive operating environment is maintained.

Fighting illicit trade

We continued to devote considerable resources to stem the illicit trade in tobacco products and engage with relevant stakeholders to ensure sustainability of industry revenues, which in turn results in sustainable Government revenues.

As part of the Business' efforts to counter illicit trade in 2017, we launched the *BAT Group Standards of Business Conduct Anti-Illicit Trade Intelligence Compliance Procedures*. Our activities to curb illicit trade in Kenya are compliant with this procedure.

To manage the challenges that exist in our supply chain in the past year, we further collaborated and co-operated with various stakeholders, including other industries faced with similar issues, the Kenya Revenue Authority (KRA), relevant law enforcement and other government agencies, in efforts to sensitise, monitor and tackle any issues arising from illicit trade in tobacco products.

CORPORATE GOVERNANCE REPORT

BOARD OF **DIRECTORS**

George Maina
Independent Non-Executive Chairman
Kenyan

POSITION: Chairman since 1 September 2013; Non-Executive Director since November 2010; and Chairman of the Nominations Committee.

SKILLS AND EXPERIENCE: George is an Engineer by profession. He worked with the Shell Group of Companies for 26 years during which time he served in Senior Management roles in Kenya, Jamaica and Ghana.

In 1998, he was appointed Managing Director of Kenya Shell and BP Kenya Ltd, before leaving corporate employment to pursue private business in 2004.

KEY APPOINTMENTS: He holds directorships in NIC Bank, Insurance Company of East Africa, Afrika Investment Bank, Faulu Kenya Limited and Nairobi Securities Exchange Ltd. He is also a Trustee of Starehe Boys Centre, Africa Conservation Centre and Gertrude Gardens Children's Hospital.

Beverley Spencer-Obatoyinbo
Executive Managing Director
British/Nigerian

POSITION: Managing Director since 2 May 2017.

SKILLS AND EXPERIENCE: Beverley most recently held the position of BAT Area Director Swiss Cluster based in Switzerland.

She joined BAT in 1996 from the pharmaceutical industry. She has held various senior roles within the BAT Group including, Marketing Director BAT Nigeria, General Manager BAT Egypt, Area Director for BAT West Africa Area and Head of Human Resources for BAT East Europe, Africa and Middle East Region.

KEY APPOINTMENTS: She is currently also the Area Director for BAT East and Central Africa Area based in Nairobi.

BOARD OF DIRECTORS

Sidney Wafula
Executive Finance Director
Kenyan

POSITION: Finance Director since 2 May 2017.

SKILLS AND EXPERIENCE: Sidney joined BAT Kenya in 2006 as Head of Audit. He has subsequently held other Senior Management, roles in Finance within the BAT Group including Head of Operations, then Marketing Finance for BAT West Africa Area based in Lagos, Head of Finance BAT Egypt and most recently Head of Finance for BAT Group's Southern Africa Markets operations, based in Mozambique until May 2017.

He is a Certified Public Accountant of Kenya and holds a Bachelor of Commerce (Accounting) Degree from the Catholic University East Africa (Kenya). He is a Member of the Institute of Certified Public Accountants of Kenya.

KEY APPOINTMENTS: He is currently also the Area Head of Finance for BAT East and Central Africa Area based in Nairobi.

Gayling May
Non-Executive Director
British

POSITION: Non-Executive Director since September 2005. Member of the Audit, Governance and Corporate Social Responsibility Committee and a Member of the Nominations Committee.

SKILLS AND EXPERIENCE: Gayling has a rich accounting background having worked for PricewaterhouseCoopers in various countries for 37 years. He is a Fellow of The Institute of Chartered Accountants in England and Wales (FCA), a Member of The Institute of Certified Public Accountants of Kenya (CPA) and a Member of The Institute of Certified Public Secretaries of Kenya (CPS).

He is currently the Regional Representative of the Eastern Africa Association, a business information service based in Nairobi, but active throughout East Africa.

KEY APPOINTMENTS: He holds directorships in Swissport Kenya Limited, Liberty Kenya Holdings Limited, Liberty Life Assurance Kenya Limited, and The Heritage Insurance Company Kenya Limited.

BOARD OF DIRECTORS

Carol Musyoka
Non-Executive Director
Kenyan

POSITION: Non-Executive Director since February 2011 and a Member of the Audit, Governance and Corporate Social Responsibility Committee.

SKILLS AND EXPERIENCE: Carol is a Lawyer by profession. She has over 10 years of Financial Leadership and Legal experience working in Kenya and the United States. Her Executive Management experience includes her role as the Corporate Director of Barclays Bank of Kenya Ltd.

She currently provides consulting and training services for various local and international commercial banks and insurance companies. She is also a popular weekly columnists in the Business Daily.

KEY APPOINTMENTS: She is Non-Executive Director of East African Breweries Limited, Kenya Airways Limited and chairs the Board of, the recently constituted, the Business Registration Services under the Attorney General's Office.

Mahmud Jan Mohamed
Non-Executive Director
Kenyan

POSITION: Non-Executive Director since November 2012. Member of the Audit, Governance and Corporate Social Responsibility Committee.

SKILLS AND EXPERIENCE: Mahmud is currently the Managing Director for Serena Hotels Africa and head of the Tourism Department of the Aga Khan Fund for Economic Development (AKFED). He is responsible for 35 Hotels, Lodges and Safari resorts located in nine countries in Africa and Asia.

His work experience includes Senior Management positions in Europe and Africa.

KEY APPOINTMENTS: He is the Founding Chairman of the Kenya Tourism Federation and a Trustee of the East African Wildlife Society. He is also a member of the Eastern Africa Association Advisory Board.

BOARD OF **DIRECTORS**

Teddy Mapunda
Non-Executive Director
Tanzanian

POSITION: Non-Executive Director since October 2014 and a Member of the Remunerations Committee.

SKILLS AND EXPERIENCE: Teddy is the founder of Montage Limited, a multi-dimensional consultancy and creative agency based in Dar-es-Salaam, Tanzania. She has over twenty years of leadership experience in public relations, customer service, administration, and sales.

She is a graduate of the Swedish Institute of Public Administration and the Ghana Institute of Management and Public Administration.

KEY APPOINTMENTS: She is Vice Chairperson for the Road Safety Committee Kinondoni Region, Tanzania, Board Member of Why Africa Now of the USA, TPS Eastern Africa (Serena Hotels), WAMA Foundation and the Arusha International Conference Centre (AICC).

Peter Mwangi
Non-Executive Director
Kenyan

POSITION: Non-Executive Director since February 2015. Chairman of Remunerations Committee and Member of the Nominations Committee.

SKILLS AND EXPERIENCE: Peter is currently the Chief Executive Officer of the UAP Old Mutual Group in East Africa. Before this appointment, he was the Chief Executive Officer of the Old Mutual Group in Kenya from October 2014. He previously served as the Chief Executive Officer of the Nairobi Securities Exchange Limited for a period of 6 years to September 2014. Prior to this, he was the Chief Executive Officer of Centum Investment Company Plc between 2004 and 2008.

He has over twenty years of proven business and leadership experience. He holds a Bachelor of Science degree in Electrical Engineering from the University of Nairobi and is also a CFA® charter holder. Additionally, he is a member of ICPAK, ICPSK and KIM.

KEY APPOINTMENTS: He serves on the Board of Directors of the Central Depository and Settlement Corporation (CDSC), Funguo Investments Limited and as an Executive Director on the boards of several subsidiaries of the UAP Old Mutual Group in East Africa.

BOARD OF DIRECTORS

Dr. Martin Oduor-Otieno
Non-Executive Director
Kenyan

POSITION: Non-Executive Director since August 2016 and a Member of the Audit, Governance and Corporate Social Responsibility Committee.

SKILLS AND EXPERIENCE: Martin is currently an independent Business Advisor and Executive Coach. Prior to this he worked with Deloitte East Africa as Partne and he also worked in the Financial Service Industry from May 2013 to December 2015.

He had an illustrious career at Kenya Commercial Bank Group between October 2005 and December 2012, initially as Deputy CEO and then as Chief Executive Officer. He has held Senior positions in Barclays Bank of Kenya Limited and in the Public Sector.

He holds an Executive MBA and Bachelor of Commerce degrees and is an alumnus of the Harvard Business School's AMP. He is a Fellow of the Kenya,Institute of Bankers, Institute of Certified Public Accountants of Kenya, a Member of the Institute of Certified Public Secretaries of Kenya and the Institute of Directors of Kenya.

KEY APPOINTMENTS: He holds Directorships in Standard Bank Group, Standard Bank of South Africa, East African Breweries Limited, Kenya Airways Limited and GA Life Assurance Limited.

Ruth Ngobi
Company Secretary
Kenyan

POSITION: Company Secretary since August 2002.

SKILLS AND EXPERIENCE: Ruth was educated in both Kenya and the UK and qualified as a lawyer in 1985. She previously worked with Unilever Kenya Limited for 15 years as Company Secretary before joining BAT Kenya in 2002 as Company Secretary and Area Legal Counsel. She retired from full time employment with BAT Kenya in 2010 but retained her role as Company Secretary.

She founded Cosec Solutions which provides Company secretarial services and corporate governance solutions to various companies.

KEY APPOINTMENTS: She is a Non-Executive Director on the Boards of Stanbic Bank Limited, Stanbic Holdings Limited and SBG Securities Limited.

DUNHILL
TOBACCO *of* LONDON LIMITED

DUNHILL RANGE

18 AND ABOVE ONLY

Sale of tobacco products to any person under the age of eighteen (18) is prohibited by law

WARNING: SMOKING HARMS PEOPLE NEXT TO YOU
ONYO: UVUTAJI WA SIGARA HUDHURU WATU WALIO KARIBU NAWE

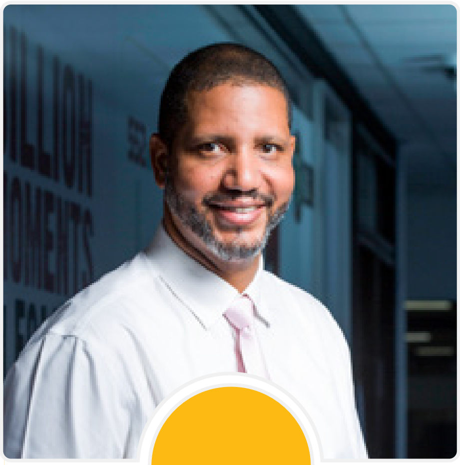
LEADERSHIP TEAM

Seyi Adeyemo
Head of Operations

Seyi joined BAT in 2013 from Procter and Gamble. He has extensive experience in Supply Chain Operations Management and Lean Six-Sigma.

Prior to his current appointment, he worked with BAT South Africa as Area Head of Supply Chain where he demonstrated strong leadership and led the transformation and integration of the primary and secondary supply chain.

Seyi is also the Area Head of Operations for BAT East and Central Africa Area based in Nairobi.



Darryn Bassa
Head of Marketing

Darryn joined BAT South Africa in 2013 as Marketing Manager, having previously worked for Unilever and in the Telecom industry for 12 years.

He has vast experience in Brand and Customer Management, with a solid background in delivering marketing strategies and trade / category plans with some of the biggest FMCG firms globally.

Prior to joining BAT Kenya in 2016, he was Senior International Brand Manager for Dunhill based in London.

Darryn is also the Area Head of Marketing for BAT East and Central Africa Area based in Nairobi.

Razeeah Belath
Head of Human Resources

Razeeah has a wealth of experience in HR Management, having worked with BAT Group for 16 years.

She joined BAT Mauritius as a Management Trainee-HR in 2001 (BAT Mauritius) and has since held various Head of HR roles in La Reunion, Angola and Indian Ocean Islands (IOI) Cluster. Razeeah has also held HR Specialist roles as above market Talent and Organisational Effectiveness Manager in Sub-Saharan Africa, Africa Middle-East, Eastern Europe Africa and Middle East in the Group's Head Office.

Razeeah is also the Area Head of HR for BAT East and Central Africa Area based in Nairobi.

LEADERSHIP TEAM

Simukai Munjanganja
Head of Legal and External Affairs

Simukai is a corporate lawyer and business executive with over 19 years of experience managing Legal, Corporate and Regulatory issues.

He joined the BAT group in Zimbabwe in 2000, where he held several roles including, Company Secretary and Legal Manager Zimbabwe and Head of Legal, Corporate and Regulatory Affairs Malawi, Mozambique, Zambia and Zimbabwe.

Prior to joining BAT Kenya, he was Global Regulation Counsel based in London.

Simukai is also the Area Head of Legal and External Affairs for BAT East and Central Africa.

Beverley Spencer – Obatoyinbo
Managing Director

Beverley has a wealth of experience in Leadership and General Management.

Having joined BAT Group in 1996, she has held various Senior roles within the BAT Group including, General Manager BAT Egypt, Area Director for BAT West Africa Area and Area Director Swiss Cluster based in Switzerland, which is her immediate former role prior to joining BAT Kenya in May 2017.

Beverley is also the Area Director for BAT East and Central Africa Area based in Nairobi.

Sidney Wafula
Finance Director

Sidney has been with BAT Group for 12 years.

He joined BAT Kenya as Head of Audit in 2006 and has subsequently held various senior Finance Management roles within the Group, including, Head of Operations Finance and Marketing BAT West Africa Area, Head of Finance BAT Egypt based in Cairo and most recently Head of Finance for BAT Group's Southern Africa Markets operations, based in Mozambique until his return to Kenya in 2017.

Sidney is also the Area Head of Finance for BAT East and Central Africa Area based in Nairobi.

Darryn Bassa, Head of Marketing awarding Dennis Irungu, Trade Marketing Representative with the POSITIVE certification in the 2018 graduation ceremony

GOVERNANCE AUDITOR'S REPORT

STATEMENT OF THE RESPONSIBILITY OF DIRECTORS

The Board is responsible for putting in place governance structures and systems that support the practice of good governance in the organisation. This responsibility includes planning, designing and maintaining governance structures through policy formulation, that is necessary for efficient and effective governance of the organisation. The Board is also responsible for ethical leadership, risk governance and internal control, transparency and disclosure, equitable protection and exercising of members' rights and obligations, compliance with laws and regulations, sustainability, performance management and strategy formulation and oversight.

The Board of Directors of British American Tobacco Kenya plc ("the Company") is committed to the highest standards of good Corporate Governance and strives for continuous improvement by identifying any loopholes and gaps in the Company's governance structures and processes. It is on this premise that the Board commissioned a governance audit, with the aim of ensuring that all processes necessary for directing and controlling the Company are in place.

The Directors have therefore ensured that the Company has undergone a governance audit for the year ended 31 December 2017, and obtained a report, which discloses the state of governance within the Company.

GOVERNANCE AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on the existence and effectiveness of governance instruments, policies, structures, systems and practices in the organisation, in accordance with best governance practices as envisaged within the legal and regulatory framework. We conducted our audit in accordance with ICPSK Governance Audit Standards and Guidelines, which conform to global standards. These standards require that we plan and perform the governance audit to obtain reasonable assurance on the adequacy and effectiveness of the organisation's policies, systems, practices and processes. The audit involved obtaining audit evidence on a sample basis. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a reasonable basis for our opinion.

Being the inaugural audit, the auditor has endeavoured to lay the groundwork for an on-going governance compliance program, in order to ensure that the Board's goals, structure and operations are consistent with the latest developments in Corporate Governance. The structure of the report, findings and recommendations will therefore focus on providing a baseline as opposed to strictly following the seven steps of governance auditing.

OPINION

In our opinion, the Board has put in place a sound governance framework, which is in compliance with the legal and regulatory framework and in line with global best governance practices for the interest of stakeholders. In this regard, we issue an unqualified opinion.

FCS. Catherine Musakali, ICPSK GA. No 006
For Dorion Associates
Date: 27 March 2018

LEADERSHIP AND RESPONSIBILITIES

Overview

Corporate governance refers to the structures and processes guiding the leadership of the Company. The Company has instituted systems to ensure that high standards of corporate governance are maintained at all levels of the organisation.

Throughout the year ended 31 December 2017 up to the date of this document, the Company endeavoured to comply with the Capital Markets Authority (CMA) Code of Corporate Governance Practices for Issuers of Securities to the Public 2015 (the Code). The Board considers that this Annual Report and notably this section provides the information shareholders need to evaluate how the Company has done so far.

Besides complying with the Code, the Company has committed to embed internal rules of engagement to support corporate governance. These internal guidelines are constituted in the Standards of Business Conduct to which every employee and the Board makes a commitment to comply with.

The role of the Board

The Board is comprised of seven (7) Non-Executive Directors including the Chairman and two Executive Directors. The Board is collectively responsible for the Company's vision and strategic direction, its values, and its governance. The Board is accountable to the Company's shareholders for the performance of the business and the long-term success of the Company. It provides the leadership necessary for the Company to meet its performance objectives within a framework of internal controls.

The key responsibilities of the Board include:

- Approving company strategy;
- Approving company policies;
- Approving major corporate activities;
- Approving the Annual Report;
- Agreeing on governance framework;
- Agreeing on company budget;
- Agreeing on Board succession plans;
- Reviewing risk management and internal controls;
- Reviewing periodic financial reports;
- Declaring interim/recommending final dividend;

The Board has established three principal Board Committees, to which it has delegated certain responsibilities namely, the Nominations Committee, the Audit, Governance and Corporate Social Responsibility Committee and the Remunerations Committee. The roles, membership and activities of these Committees are described in more detail later in this Report. Each Committee has its own terms of reference which are reviewed annually and updated as appropriate.

Division of responsibilities

The Chairman and Managing Director are responsible for the profitable operation of the Company. Their roles are separate, with each having distinct and clearly defined duties and responsibilities.

The Chairman is responsible for the leadership of the Board, for ensuring its effectiveness on all aspects of its role and for facilitating the productive contribution of all Directors. He sets the agenda for Board meetings in consultation with the Managing Director and the Company Secretary. He is also responsible for ensuring that the interests of the Company's shareholders are safeguarded and that there is effective communication with them. The Chairman is accountable to the Board for leading the direction of the Company's corporate and financial strategies and for the overall supervision of the policies governing the conduct of the business.

The Managing Director has overall responsibility for the performance of the business. She provides leadership to facilitate successful planning and execution of the objectives and strategies agreed by the Board. She is also responsible for stewardship of the Company's assets and jointly with the Chairman, cater to the representation of the Company externally.

Non-Executive Directors

The Board had seven (7) Non-Executive Directors as at 31 December 2017 and as at the date of this Annual Report. The role of the Non-Executive Directors is to help develop strategy, review Management proposals, scrutinise the Management performance, bring an external perspective to the Board, monitor performance reporting and be available to meet with major shareholders as appropriate.

Board programme

The Company's annual Board programme is designed to enable the Board to drive the strategy forward across all the elements of the Company's business model. The key activities of the Board in 2017, grouped under the Company's four strategy pillars, are set out on page 51.

The Board devotes considerable attention to corporate governance matters relating to the Company's internal controls and compliance activities. It receives verbal updates from the Chairman of the Audit Committee following each Committee meeting as well as the full minutes.

Information and support

The Board receives high-quality, up to date information for review in good time ahead of each meeting. The Company Secretary ensures timely information dissemination within the Board and its Committees and between the Non-Executive Directors and senior management as appropriate.

The Leadership Team

The Leadership Team led by the Managing Director is responsible for overseeing the implementation of the strategy and policies set by the Board, and for creating the framework for their successful day-to-day operations. Their profiles are set out on pages 44 to 45 of this Annual Report.

Principal Leadership Team role includes:

- Developing strategy for approval by the Board;
- Developing guidelines for the Company's functions;
- Ensuring functional strategies are effective and aligned;
- Managing functions;
- Reviewing functional budgets;
- Monitoring Company operating performance;
- Overseeing the management and development of talent;

The composition of the Board

The composition of the Board as at 31 December 2017 and as at the date of this Annual Report is set out on page 7.

Board and AGM meeting attendance in 2017

Name	Attended/Eligible to attend
George Maina	5/5
Beverley Spencer-Obatoyinbo[1]	2/2
Sidney Wafula[2]	2/2
Gayling May	5/5
Carol Musyoka	4/5
Mahmud Jan Mohamed	3/5
Teddy Mapunda	4/5
Peter Mwangi	4/5
Dr. Martin Oduor-Otieno	5/5
Ruth Ngobi	5/5

1. Beverley Spencer-Obatoyinbo was appointed Managing Director effective 2 May 2017 following the resignation of Keith Gretton on 1 st May 2017 as Managing Director.

2. Sidney Wafula was appointed Finance Director effective 2 May 2017 following the resignation of Philip Lopokoiyit on 1 May 2017 as Finance Director.

Financial and Business Reporting

The Board is satisfied that it has met its obligation to present a balanced and understandable assessment of the Company's position throughout the Annual Report. It is appropriate to treat this business as a going concern as there is sufficient existing financing available to meet expected requirements in the foreseeable future. The Audit, Governance and Corporate Social Responsibility Committee is assigned to review the financial, audit and internal control issues in supporting the Board of Directors, which is responsible for the financial statements and all information in the Annual Report.

Risk Management and Internal Control

The Board is responsible for determining the nature and extent of the significant risks that the Company is willing to take to achieve its strategic objectives and for maintaining sound risk management and internal control systems. With the support of the Audit, Governance and Corporate Social Responsibility Committee the Board carries out a review of the effectiveness of its risk management and internal control systems annually, covering all material controls including financial, operational and compliance controls and risk management systems.

Risk registers, based on a standardised methodology, are used to identify, assess and monitor the key risks (both financial and non-financial) faced by the business. Information on prevailing trends, for example, whether a risk is considered to be increasing or decreasing over time, is provided in relation to each risk and all identified risks are assessed at three levels (high/medium/low), by reference to their impact and likelihood. Mitigation plans are put in place to manage the risks identified and the risk registers while mitigation plans are reviewed on a regular basis.

The Company also completes a checklist of the key controls annually in compliance with the Group best practice, known as the Control Navigator. Its purpose is to enable self-assessment in the internal control environment, and to assist in identifying any controls which may require strengthening and monitoring action plans, to address control weaknesses. The Control Navigator checklist is reviewed annually to ensure that it remains relevant to the business and covers all applicable key controls.

The Board, with advice from the Audit, Governance and Corporate Social Responsibility Committee, has completed its annual review of the effectiveness of the system of risk management and internal control for the period since 1 January 2017. No significant failings or weaknesses were identified and the Board is satisfied that, where specific areas for improvement have been identified, processes are in place to ensure that the necessary remedial action is taken and that progress is monitored.

BOARD EFFECTIVENESS

Balance and diversity

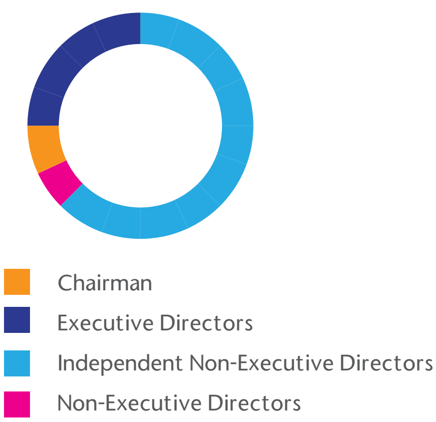
A balanced Board

Our Non-Executive Directors come from broad industry and professional backgrounds, with varied experience and expertise aligned with the needs of our business. Women constitute 33% of our Board. Short biographies of the Directors, including details of their relevant skills, experience, and nationalities, are set out in the Board of Directors pages in this section (pages 38 to 42).

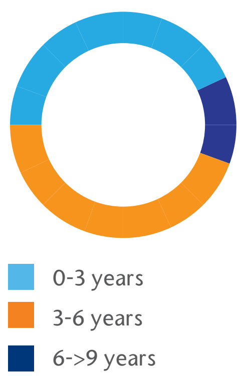
Promoting diversity

The Board appreciates the benefit of diversity in all its forms, within its own membership and at all levels of the Company. The Board promotes diversity and encourages initiatives to improve gender diversity in Senior Management roles. The Boards Diversity Policy can be read on the Company's website (www.batkenya.com).

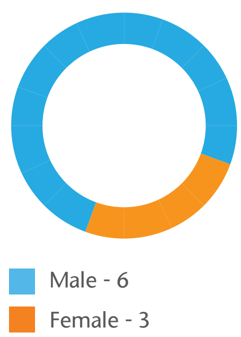
Balance of Non-Executive Directors and Executive Directors



Length of tenure of Non-Executive Directors



Gender split of Directors



Independence and conflicts of interest

Independence

The Chairman and five (5) of the Non-Executive Directors are Independent as defined in the Code and accordingly, the majority of the Board is constituted of Independent Directors.

Conflicts of interest

The Board has formal procedures for managing conflicts of interest in accordance with the Companies Act 2015 and the CMA Code of Corporate Governance Practices for Issuers of Securities to the Public and may authorise situational conflicts under the Company's Articles of Association.

Directors are required to give advance notice of any conflict issues to the Chairman or Company Secretary and these are considered at the next Board meeting.

Declaration of conflicts of interest is also the first agenda item of all Board meetings. Directors are excluded from the quorum and vote in respect of any matters in which they have an interest. No material conflicts were reported by Directors in 2017.

Information and professional development

Board induction

On joining the Board, all Directors receive a full induction. Non-Executive Directors also receive a full programme of briefings on all areas of the Company's business from the Executive Directors, members of the Leadership Team, the Company Secretary and other senior executives. The induction includes a factory tour and a market visit.

Following their appointments on 2 May 2017, both Beverley Spencer-Obatoyinbo and Sidney Wafula, received a comprehensive induction to the operations of the Company to enable them to effectively take up their roles and execute their responsibilities.

Training and development

Functional presentations are built into the annual Board work plan, so that Non-Executive Directors gain a good sense of the Company's operations and central functions. The Non-Executive Directors are also invited to attend scheduled market visits so that they gain exposure to the Company's business on the ground.

The Board and its Committees receive regular briefings on legal and regulatory developments with particular emphasis on regulations that directly impact the operations of the Company.

The Chairman meets each Non-Executive Director individually to discuss their individual training and development plans. During 2017, each Director was able to secure more than twelve hours of training on areas of governance from the Company and other credible sources as prescribed by the CMA Code of Corporate Governance Practices for Issuers of Securities to the Public, 2015.

Shareholder engagement

The AGM is an opportunity for shareholder engagement and for the Chairman and the Managing Director to explain the Company's full year performance and to receive questions from shareholders. The Chairmen of the Audit, Governance and Corporate Social Responsibility Committee, Nominations and Remunerations Committees are normally available at the AGM to take any relevant questions, with all other directors in attendance, unless illness or pressing commitments preclude them from doing so.

The Company holds investor briefs twice a year. This facilitates engagement with key stakeholders from the Nairobi Securities Exchange, Capital Markets Authority and various fund managers representing institutional and foreign investors. The Managing Director and Finance Director are among the Senior Management on hand at investor briefs, to respond to stakeholder queries.

In 2015, the Company introduced Shareholders "Open Day". The same was conducted on 5 April 2017. Shareholders in attendance were taken through the Company's operations at the Green Leaf Processing Plant in Thika and also participated in a tour of the plant.

During the AGM held in April 2017 and at the two investor briefs held in February and July 2017, shareholders and stakeholders were keen to hear more on the latest developments in industry regulation. Excise increases (and the related issue of increased illicit trade) were also regular topics as was the request from shareholders at the AGM for consideration of a bonus share issue or share split.

Board evaluation

Evaluation process

A critical evaluation of the effectiveness of the Board and its committees, the Executive and Non-Executive Directors, the Chairman and the Company Secretary for the preceding year is conducted as prescribed by the CMA Code of Corporate Governance Practices for Issuers of Securities to the Public.

The evaluation is conducted by each Director completing a Board Effectiveness Evaluation form. Respondents are requested to rank the Board against several outcomes. They also have the opportunity to elaborate their replies by providing specific comments. This information is thereafter collated by the Company Secretary and presented to the Nominations Committee with a view to identifying and recommending areas for improvement. The findings from the Board Evaluation exercise are subsequently presented to the full Board and recommendations for improvements discussed and if thought fit, approved.

The evaluation for 2016 was conducted in 2017. All Executive and Non-Executive Directors participated in the evaluation process.

A report was prepared for the Board on the results of this exercise. The results of the evaluation show that the Board continues to function well and each of its committees continues to be efficient and effective, with demonstrated progress against 2015 actions and recommendations.

The wide range of skills and diverse backgrounds of members is a key strength of the Board, as is effective leadership from the Chairman and the collegiate atmosphere. Board members have a good understanding of the business and receive the information they need to inform decisions.

The above notwithstanding, recommendations and fresh actions points were identified for implementation.

Constructive feedback

Individual feedback was given by the Chairman to all Board members. All Board members continued to perform well, and each was considered to be making an effective contribution to the Board.
Feedback on the Chairman's own performance was given to him by the Nominations Committee.

Governance audit

In compliance with the CMA Code of Corporate Governance Practices for Issuers of Securities to the Public 2015, the Board appointed Ms. Catherine Musakali, of Dorion Associates LLP, to conduct the Company's 2017 Governance Audit. The Report of the Independent Governance Auditor is set out on page 47.

STRATEGIC BOARD ACTIVITIES IN 2017

Growth

Growth remains the Board's key strategic focus. Continued investment in our strategic focus areas is central to the Board's annual agenda.

Activities in 2017

- Reviewing and agreeing on a re-articulation of the Company's strategy;
- Satisfying itself throughout the year, that Management was on track to deliver the Company's strategy, and endorsing the direction and activities proposed by Management to achieve its strategic metrics;
- Considering the Company's innovation pipeline for its brands in light of new consumer trends and insights, and how planned innovations can help strengthen its product portfolio;
- Keeping the Company's trading performance under review, particularly the performance of the Company's key local brand, Sportsman, and its Global Drive Brands;
- Discussing and improving the Board's understanding of key risks facing the Company; and
- Considering the potential impact on the business of specific risk factors in consultation with the Audit, Governance and Corporate Social Responsibility Committee.

Delivering growth

In September 2017 the Board held a one day off-site meeting with the Leadership Team, to approve the 2018 Company Plan and Budget.

New marketing insights and how these were informing brand development plans and driving the Company's innovation pipeline were shared.

The Company's integrated product and leaf strategy was discussed, as was cost management initiatives and strategic drivers to enable collaborative and efficient ways of working.

Productivity

The Board pays close attention to the Company's operational efficiency, cost and capital effectiveness.

Activities in 2017

- Monitoring operational key performance indicators;
- Implementation of Graphic Health Warning packaging;
- Operations Transformation, including Integrated Work Systems roll-out, above market synergies for logistics and materials planning;
- Review of additional volume from contract manufacture;
- Discussing strategic direction of leaf supply and farmer earnings;
- Safety at both Nairobi and Thika factories, with the Business Continuity Plan strengthened against the prolonged electioneering period in 2017;
- Capacity and capability upgrades in the factory; and
- Savings and productivity opportunities.

Sustainability

The Board places considerable emphasis on the need for the business to be sustainable for the long term, to meet the expectation of stakeholders and inform the Company's commitments to society.

Activities in 2017

- Reviewing the Company's regulatory strategy in the context of the current regulatory landscape, including graphic health warnings directives, the plastic ban and the potential implication for the business;
- Monitoring the status of the Company's litigation proceedings, including updates on the Kenya Tobacco Control Regulations challenge case which commenced in April 2015;
- Environmental, health and safety performance; and
- Monitoring compliance with the Company's Standards of Business Conduct and internal controls. A number of allegations were made towards the end of 2015 regarding historical misconduct. The Board instructed that it be kept updated on findings on the allegations.

Winning Organisation

Setting the 'tone from the top' is an important part of the Board's role which helps to foster a culture centered around the Company's guiding principles, and harness diversity.

Activities in 2017

- Reviewing succession planning at Board Level including Executive Directors and the Leadership Team and monitoring the progress of Leadership Team development plans;
- Receiving updates on the difficulties of attracting and retaining talent and factoring this into consideration of revised talent and remuneration policies;
- Reviewing the application and continuing impact of the Remuneration Policy during 2017;
- Reviewing the development of leaders in the Company, in particular activities that drive a high-performance leadership culture;
- Receiving updates on the Collective Bargaining Agreement negotiations with the Union; and
- Considering Executive Director appointment proposals and appointing the new Managing Director and Finance Director in May 2017.

BOARD COMMITTEES

Nominations Committee

Current Members

George Maina
Gayling May
Peter Mwangi
Mahmud Jan Mohamed
Ruth Ngobi (Secretary)

Attendance at meetings in 2017

Name	Attended/Eligible to attend
George Maina	1/1
Gayling May	1/1
Peter Mwangi	1/1
Mahmud Jan Mohamed	0/1
Ruth Ngobi (Secretary)	1/1

Mandate and role of the Nominations Committee

The mandate of the Nominations Committee is to make recommendations to the Board on the suitability of candidates for appointment to the Board. In so doing, the Committee reviews the structure, size and composition of the Board to ensure it has an appropriate balance of skills, expertise, knowledge and independence. It ensures that the procedure for appointing Directors is rigorous, transparent, objective, merit-based and has regard for diversity.

The process includes an evaluation of the skills and experience being sought prior to recruitment. The selection process generally involves interviews with prospective candidates by the Chairman and committee members. In so doing, it monitors and ensures that appropriate Non-Executive and Executive Directors' ratios are maintained.

The committee also evaluates and makes recommendations with regard to the composition of all Board committees.

This committee is also charged with the responsibility of evaluating and reporting to the Board on an annual basis, the effectiveness of the Board and of the Directors in the discharge of their responsibilities.

Following the introduction of compliance reporting by the CMA, the Committee provides oversight of implementation of the new Code and Compliance Reporting. For the Committee's terms of reference visit www.batkenya.com.

Key Nominations Committee activities in 2017

- Reviewing succession planning for the Board and the Leadership Team;
- Considering the resignations of Keith Gretton and Philip Lopokoiyit as Managing Director and Finance Director respectively effective 1 May 2017 and the proposed appointments of Beverley Spencer-Obatoyinbo and Sidney Wafula;
- Directors' annual appointment and re-election at the AGM;
- Reviewing the Corporate Governance Report for the 2017 Annual Report;
- Reviewing the composition of Board committees and recommending to the Board the appointment of Dr. Martin Oduor-Otieno as Chairman of the Audit, Governance and Corporate Social Responsibility Committee with effect from November 2017;
- Reviewing the effectiveness of the Board and its Committees, following the Board evaluation exercise and making recommendations to the Board on actions to be adopted towards improvement;
- CMA corporate governance compliance reporting requirements;
- Review of the Board's diversity policy and the Nominations Committee's terms of reference.

Terms of appointment to the Board

The Non-Executive Directors do not have service contracts with the Company, but instead have letters of appointment for an initial term of two (2) years. The Board takes into account the need for it to refresh its membership progressively over time. Letters of appointment are renewable after the initial two (2) years, as per the Board's policy on tenure and upon recommendation by the Nominations Committee.

The letters of appointment of the Non-Executive Directors are available for inspection at the registered offices of the Company upon notice.

Re-election of Directors

In accordance with the Articles of Association of the Company, all Directors offer themselves for re-election at regular intervals, subject to continued satisfactory performance and commitment. All new appointments to the Board are subject to election by shareholders at the first Annual General Meeting, after their appointment.

At this year's AGM on 11th May 2018, the Company will be submitting all eligible Directors for re-election and, in the case of Beverley Spencer-Obatoyinbo and Sidney Wafula, election for the first time.

The Nominations Committee confirms that the performance of the Non-Executive Directors being proposed for re-election continues to be effective and that they continue to demonstrate commitment to their roles including, committing the necessary time for Board and Committee meetings and other duties.

The Audit, Governance and Corporate Social Responsibility Committee (The Audit Committee)

Current Members

Dr. Martin Oduor-Otieno (Chairman)
Gayling May
Carol Musyoka
Mahmud Jan Mohamed
Cecil Leperrier (Secretary)[2]

Attendance at meetings in 2017

Name	Attended/Eligible to attend
Dr. Martin Oduor-Otieno[1]	5/5
Gayling May	5/5
Carol Musyoka	4/5
Mahmud Jan Mohamed	4/5
Cindy Albertyn (Secretary)[2]	3/5

1. Dr. Martin Oduor-Otieno was appointed Chairman of the Committee effective November 2017.
2. Cindy Albertyn resigned on 7 November 2017 and was immediately replaced by Cecil Leperrier.

Mandate and role of the Audit Committee

The Audit Committee is responsible for monitoring the integrity of the financial statements and any formal announcements relating to the Company's performance, considering any significant issues and judgements reflected in them before submission to the Board. The Committee keeps under review the consistency of the accounting policies applied by the Company, reviews the effectiveness of the accounting, internal control and business risk systems of the Company and, when appropriate, makes recommendations to the Board on business risks, internal controls and compliance.

The Committee is also responsible for monitoring compliance with the Company's Standards of Business Conduct, monitoring and reviewing the effectiveness of the Company's internal audit function; and monitoring and reviewing the performance of the Company's external auditors, by keeping under review their independence and objectivity, making recommendations as to their reappointment (or, where appropriate, making recommendations for change), and approving their terms of engagement and the level of audit fees payable to them.

The Board has an obligation to establish formal and transparent arrangements for considering, how it should apply the corporate reporting, risk management and internal control principles, and for maintaining an appropriate relationship with the external auditors, which are delivered through the Audit Committee.

The Audit Committee is also responsible for monitoring and reviewing the effectiveness of the internal audit function. The Internal Audit Manager is a permanent invitee to the committee. The Internal Audit Manager presents a report to the Committee on the audit plan for the year, as well as updates on ongoing and completed audits. Further, the Audit Committee meets separately with the internal audit team and the external auditors' representatives at the end of every meeting, without Management.

Risk management and internal control

The Board is responsible for determining the nature and extent of the significant risks that the Company is willing to take to achieve its strategic objectives, and for maintaining sound risk management and internal control systems. With the support of the Audit Committee, the Board carries out a review of the effectiveness of its risk management and internal control systems annually, covering all material controls including financial, operational and compliance controls and risk management systems.

Risk registers, based on a standardised methodology, are used to identify, assess and monitor the key risks (both financial and non-financial) faced by the business. Information on prevailing trends, for example, whether a risk is considered to be increasing or decreasing over time, is provided in relation to each risk and all identified risks are assessed at three levels (high/medium/low) by reference to their impact and likelihood. Mitigation plans are put in place to manage the risks identified and the risk registers and mitigation plans are reviewed on a regular basis.

The Company also completes a checklist of the key controls annually in compliance with the BAT Group best practice, known as the Control Navigator. Its purpose is to enable self-assessment in the internal control environment, and to assist in identifying any controls which may require strengthening and monitoring action plans, to address control weaknesses. The Control Navigator checklist is reviewed annually to ensure that it remains relevant to the business and covers all applicable key controls.

The Board, with advice from its Audit Committee, has completed its annual review of the effectiveness of the system of risk management and internal control for the period since 1 January 2017. No significant failings or weaknesses were identified and the Board is satisfied that, where specific areas for improvement have been identified, processes are in place to ensure that the necessary remedial action is taken and that progress is monitored.

Key Audit Committee activities in 2017

Agenda items considered by the Committee:

- The Company's 2017 full year and 2017 half year financial results;
- The external auditors' report;
- Progress on 2017 internal audit plan;
- Updates from the Internal Audit Manager on both Local and Global process audits, the Management Responses and plans being put in place to address any concerns raised;
- Updates on quarterly risk heat map, including deep dives into specific risk topics;
- Quarterly reports on security risks, frauds and losses;
- Updates on regulatory developments, significant legal cases, Environment, Health and Safety issues;
- Reports on compliance with the Company's Standards of Business Conduct;
- Changes to 2017 year-end Audit Report to meet, requirements of the new Companies Act, 2015;
- 2017 external auditors' work plan;
- Annual review of external auditors' independence;
- 2018 internal audit plan; and
- Reviewing and assessing compliance with the CMA Corporate Governance Practices for Issuers of Securities to the Public 2015.

External auditors

KPMG Kenya are the Company's external auditors. The Audit Committee considers that its relationship with the auditors worked well during the period and was satisfied with their effectiveness. The external auditors are required to rotate the audit partner responsible for the Company's audit at least every five years. The current lead audit partner has been in the position since 5 May 2015 when KPMG Kenya was appointed as external auditor by Shareholders.

Standards of Business Conduct (SoBC)

All BAT Kenya employees and members of the Board are expected to live up to the Standards of Business Conduct and guidance is provided through training and awareness programmes.

Every employee and members of the Board sign a declaration to comply with the Standards of Business Conduct annually. The Standards of Business Conduct also set out the Group's whistleblowing policy, which enables staff, in confidence, to raise concerns about possible improprieties in financial and other matters, and to do so without fear of reprisal, provided that such concerns are not raised in bad faith.

Any whistleblowing incidents are tabled at the Audit Committee. The procedures in place ensure an independent investigation and appropriate follow-up actions. The Standards of Business Conduct are available on www.batkenya.com.

Remuneration Committee

Current Members

Peter Mwangi (Chairman)
Teddy Mapunda
Beverley Spencer-Obatoyinbo
Sidney Wafula
Carol Musyoka
Razeeah Belath (Secretary)

Attendance at meetings in 2017

Name	Attended/Eligible to attend
Peter Mwangi (Chairman)	2/2
Teddy Mapunda	1/2
Carol Musyoka	2/2
Razeeah Belath (Secretary)	2/2

Mandate of the Remuneration Committee

The Remuneration Committee considers the remuneration policy annually for employees, Executive and Non-Executive Directors. The Remuneration Committee ensures that the remuneration policy is aligned with business needs, is performance-driven and appropriately benchmarked against other companies in Kenya.

The Remuneration Committee is responsible for:

- Setting executive remuneration policies covering salary and benefits, performance-based variable rewards, pensions and the terms of service contracts;
- Determining, within the terms of the agreed policy, the specific remuneration packages for the Chairman, the Executive Directors and the Non-Executive Directors, both on appointment and on review;
- The setting of targets applicable to the Company's performance-based variable reward schemes, determining achievement against those targets, exercising discretion where appropriate and as provided by the applicable scheme rules and policy; and
- Monitoring and advising the Board on any major changes to the policy on employee benefit structures for the Company.

Key Remuneration Committee activities in 2017

- Salary survey outcome for Kenya;
- Deep dives into the comparator companies total cost of employment analysis;
- Cascade of the global remuneration strategy and principles;
- Reward proposition versus turnover of top talent; and
- Analysis of regrettable losses.

GOVERNANCE POLICIES

The BAT Kenya Board is governed by a Board Charter, which stipulates the roles and responsibilities of the Board and its members, the composition of the Board and its committees, and their respective Terms of Reference (ToR).

Information Technology policy

BAT Kenya invests heavily in information technology systems, to support the delivery of the Company's commercial goals. BAT Kenya's information technology (IT) systems are covered under an IT policy. BAT Kenya's IT Policy aims to protect the Company's investment in information technology infrastructure IT equipment and mobile facilities, data/ telecommunications networks and software, maintain the highest standards of cyber security, while protecting the Company's confidential and sensitive information.

The policy aims to facilitate ease of use of IT systems by employees, business partners and other stakeholders, while mandating the responsible use of these IT systems. In delivering on its IT objectives, BAT Kenya leverages on IT expertise within the BAT Group, taking learnings on global IT best practices and benefiting from economies of scale in purchase of IT equipment and services.

Statement on Insider Dealing

As a listed Company, BAT Kenya is obliged under the Companies Act, 2015, to require that Directors and certain other employees, with insider information, to not abuse or place themselves under suspicion of abusing insider information that they may have or thought to have. This is especially so in periods leading up to an announcement of financial results. To this end, the Company has a Code of Share Dealing policy document, which sets out the requirements for BAT Kenya insiders, in dealing in shares of the Company.

To ensure compliance with the Companies Act, 2015 in this regard, the Company communicates 'open' and 'closed' periods for trading in its shares to its employees and Directors on an annual basis. To the best of the Company's knowledge, there was no insider dealing in the BAT Kenya 2017 financial year.

Procurement policy

BAT Kenya maintains a procurement policy that governs the procurement of goods and services. This policy and the related procedures are necessary to ensure that procurement is able to generate value in the acquisition of goods and services while satisfying the needs of the business, with the exception of tobacco, salaries and strategic machinery.

The policy also ensures that the most appropriate and effective controls are applied in the purchase of goods and services for the Company's needs. The Company periodically reviews this policy as may be necessitated by market conditions, legal requirements or other factors.

Whistleblowing policy

BAT Kenya's Standards of Business Conduct (SoBC) is a statement of the Company's values in its day-to-day activities. This policy covers BAT Kenya's commitments on issues such as bribery, corruption and human rights, in addition to setting out the Company's whistleblowing procedures. The Whistleblowing policy provides the platform for employees to raise concerns regarding any suspected wrongdoing, and the policy details how such concerns are addressed.

Corporate Social Investment (CSI) and Responsibility

BAT Kenya's CSR framework is underpinned by five core beliefs:

- Creating long-term shareholder value;
- Engaging constructively with our stakeholders;
- Creating inspiring working environments for our people;
- Adding value to the communities in which we operate and that;
- Suppliers, and other business partners should have the opportunity to benefit from their relationship with us.

Our CSI strategy is derived from our belief in adding value to the communities in which we operate, and at BAT Kenya, our CSI framework focuses on Sustainable Agriculture and Environmental Conservation. As such, at least 70% of our CSI spend is driven towards this pillar (currently focusing on afforestation and biodiversity), while 30% is allocated to other relevant initiatives such as disaster/emergency relief and empowerment.

Environmental policies

BAT Kenya has a robust Environmental Health and Safety Policy, aimed at providing a safe and healthy working environment for its employees, and any other person within the Company's sphere of operations.

BAT Kenya also maintains an Energy Policy, aimed at achieving the highest practicable levels of energy conservation and reducing CO2 emissions, for the conservation of the environment and the sustainability of natural resources.

"Our business fundamentals remain strong

In 2017, BAT Kenya successfully navigated a difficult trading environment in Kenya and across our export markets to deliver a solid, albeit reduced set of results."

FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2017

DIRECTORS' REPORT

The Directors submit their report together with the audited financial statements for the year ended 31 December 2017, which disclose the state of affairs of the Group and of the Company.

Principal Activities

The principal activities of the Group are the manufacture and sale of cigarettes and tobacco.

Results and Dividend

The net profit for the year of KSh. 3,336,006,000 (2016: KSh. 4,234,334,000) has been added to retained earnings. During the year an interim dividend of KSh. 350,000,000 (2016: KSh. 350,000,000) was paid. The Directors recommend the approval of a final dividend of KSh. 2,250,000,000 (2016: KSh. 3,950,000,000).

Directors

The Directors who held office during the year and to the date of this report are set out on page 7.
The following changes have taken place in the Board of Directors since the last Annual General Meeting:

- Keith Gretton resigned as Managing Director on 1 May 2017.
- Beverley Spencer-Obatoyinbo was appointed Managing Director on 2 May 2017.
- Philip Lopokoiyit resigned as Finance Director on 1 May 2017.
- Sidney Wafula was appointed Finance Director on 2 May 2017.

In accordance with Article 102, Beverley Spencer-Obatoyinbo and Sidney Wafula retire from the Board, and being eligible, offer themselves for re-election.

George Maina, Carol Musyoka and Gayling May retire by rotation, and being eligible, offer themselves for re-election in accordance with Article 103 of the Articles of Association.

Business Overview

The decrease in the domestic market was partially offset by recovery in export volumes and revenues, following additional pricing and distribution expansion initiatives implemented during the year, and marginal price increases in contract manufacture due to inflation. Government revenues declined in line with the decline in volumes in the domestic market, but did not offset the decline in gross revenue. Consequently, net revenue decreased in line with gross revenue by 6% to KSh.18.7 billion.

The cost of operations reduced by 2.4% to KSh. 13.3 billion due to reduced volumes, stringent cost management and productivity initiatives. However, this was not enough to offset the impact of the lower domestic volumes on revenue, and an unexpected 87% increase in the cost of tax stamps announced in April 2017 as part of the Excise Act, 2017. As a result, the operating margin reduced by 2.2 percentage points to 30.8%.

The Company has continued to embed innovative ways of working using technology, primarily in the factory. As a result of these efficiency gains, the Company undertook a reorganisation in the second half of 2017 which cost KSh. 392 million. Finance costs increased to KSh. 494 million principally due to higher borrowing in the first half of 2017, to finance working capital and minimise the risk of potential supply chain disruptions.

The reduced revenues led to lower profit before and after tax.

Cash generated from operations dropped to KSh. 6.4 billion driven by lower profitability during the year offset by gains from working capital management.

Taxes in the form of Excise Duty, VAT, Pay As You Earn (PAYE) and Corporation Tax, reduced by KSh. 1.2 billion to KSh. 18 billion in 2017, as a consequence of the adverse impact of the excise-led price increase mentioned above. BAT Kenya, nevertheless, remains a leading tax contributor in Kenya.

Auditors

The auditors, KPMG Kenya, are eligible and hereby offer themselves for re-appointment in accordance with the requirements of the Kenyan Companies Act, 2015.

Relevant Audit Information

The Directors in office at the date of this report confirm that:

- There is no relevant audit information of which the Company's auditors are unaware; and
- Each Director has taken all the steps that he or she ought to have taken as a Director so as to be aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Approval of the Financial Statements

The financial statements set out on pages 68 to 102 were approved at a Meeting of the Directors held on 15 February 2018.

By order of the Board

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Ruth Ngobi
Company Secretary

Date: 15 February 2018

RIPOTI YA WAKURUGENZI

Wakurugenzi waliwasilisha ripoti pamoja na hesabu iliyokaguliwa katika mwaka iliomalizika tarehe 31 Desemba 2017, inayoonyesha hali halisi ya kundi na kampuni.

Shughuli kuu

Shughuli kuu za kundi na kutengeneza na kuuza sigara na tumbaku.

Matokeo na mgao wa faida

Faida halisi kwa mwaka ya KSh. 3,336,006,000 (2016: KSh. 4,234,334,000) imeongezwa kwa mapato pesa zilizosalia baada ya malipo ya mgao wa faida. Wakati wa mwaka huo, mgao wa faida wa muda wa KSh. 350,000,000 (2016: KSh. 350,000,000) ulilipwa. Wakurugenzi wanapendekeza kuidhinishwa kwa mgao wa mwisho wa KSh. 2,250,000,000. (2016: KSh. 3,950,000,000).

Halmashauri ya wakurugenzi

Wakurugenzi waliokuwa ofisini wakati wa mwaka huo hadi wakati wa kutolewa kwa ripoti hii wametajwa kwenye kurasa wa saba.

Mabadiliko yafwatayo yametekelezwa kwenye halmashauri ya wakurugenzi tangu mkutano mkuu wa mwaka uliopita:

- Keith Gretton alijiuzulu kama Mkurugenzi Mkuu tarehe 1 Mei 2017.
- Beverley Spencer-Obatoyinbo aliteuliwa kuwa Mkurugenzi Mkuu mnamo tarehe 2 Mei 2017.
- Philip Lopokoiyit alijiuzulu kama Mkurugenzi wa Fedha mnamo tarehe 1 Mei 2017.
- Sidney Wafula alichaguliwa kuwa Mkurugenzi wa Fedha mnamo tarehe 2 Mei 2017.

Kulingana na kifungu namba 102 Beverley Spencer-Obatoyinbo na Sidney Wafula watastaafu kutoka kwa halmashauri, lakini wanaweza kujiwasilisha kuchaguliwa tena.

George Maina, Carol Musyoka na Gayling May wanastaafu chini ya mfumo wa kupokezana lakini wanaweza kujiwasilisha kuchaguliwa tena kulingana na kifungu namba 103 ya sheria za Kampuni.

Mtazamo wa biashara

Upungufu wa mauzo katika soko la hapa nchini hata hivyo ulisawazishwa kwa kiwango kidogo na imariko la mauzo katika masoko ya nje kufuatia utekelezaji wa bei mpya na ufunguzi wa vituo ziada vya usambazaji bidhaa zetu na ongezeko ndogo la bei kwa watengenezaji kwa kandarasi kwa sababu ya ongezeko la gharama ya maisha. Ushuru kwa serikali ulipungua kwa sababu ya kufifia kwa mauzo katika soko la hapa nchini, lakini hayakusawazisha upungufu katika mapato jumla. Kwa ujumla mapato halisi yalipungua ikilinganishwa na mapato jumla kwa asilimia 6 hadi shillingi billioni 18.7.

Gharama ya shughuli za biashara ilipungua kwa asilimia 2.4 hadi shillingi billioni 13.3 kutokana na kupungua kwa mauzo, utekelezaji kanuni mpya za kupunguza matumizi na mbinu za uzalishaji. Hata hivyo, hii haikusawazisha athari za upungufu mauzo ya hapa nchini kwa mapato na nyongeza ya ghafla ya asilimia 87 ya dua ya gharama ya stampu za ushuru iliyotekelezwa mwezi Aprili mwaka 2017. Hivyo basi kulikuwa na upungufu wa asilimia 2.2 katika gharama jumla ya shughuli za biashara hadi asilimia 30.8.

Kampuni imeendelea kuvumbua na kutekeleza mbinu mpya za kufanya kazi, kwa kutumia teknolojia katika viwanda vyetu. Kufuatia manufaa yaliotokana na mbinu hizo mpya, kampuni ilifanya mageuzi katika nusu ya pili ya mwaka 2017, shughuli iliyogharimu shillingi millioni 392. Gharama ya shughuli za kifedha iliongezeka hadi shillingi millioni 494, hasa kutokana na kuongezeka kwa mikopo katika nusu ya kwanza ya mwaka 2017 kufadhili mtaji wa utendaji na pia kuepusha kuvurugika kwa mfumo wa uwasilishaji ghafi za matumizi kwa kampuni.

Mapato yaliopungua yalisababisha kupungua kwa faida kabla na baada ya kulipa ushuru

Pesa zilizopatikana kutoka kwa shughuli zetu zilipungua hadi shillingi billioni 6.4, kwa sababu ya kupungua kwa faida katika kipindi hicho, lakini, zikasawazishwa na pesa zilizookolewa kutokana na uthibiti wa gharama ya mtaji.

Ushuru wa bidhaa, ushuru ziada wa thamani, VAT, Pay As You Earn (PAYE) na ushuru wa ushirika ulipungua kwa shillingi billioni 1.2 hadi shillingi billioni 18 katika mwaka 2017, kwa sababu ya nyongeza ya bei ya sigara kutokana na kuongezeka kwa ushuru wa sigara iliyotajwa awali. Hata hivyo, Kampuni ya BAT Kenya, ingali inaongoza katika malipo ya ushuru hapa nchini.

Wakaguzi wa hesabu

Wakaguzi wa hesabu, KPMG Kenya, wana utahilifu na wanajiwasilisha kuchaguliwa tena kuambatana na masharti na kanuni za sheria ya kampuni ya mwaka 2015.

Maelezo ziada kuhusu ukaguzi

Wakurugenzi waliokuwa ofisini kufikia tarehe ya kutayarishwa kwa ripoti hii wanathibitisha kwamba:

- Hakuna maelezo yanayohusu ukaguzi wa hesabu, ambayo wakaguzi wa hesabu wa kampuni hawafahamu; na
- Kila mkurugenzi amechukua hatua zote anahitajika kuchukua kama mkurugenzi kujifahamisha kuhusu maswala yote yanayohusu ukaguzi na kuhakikisha kuwa maelezo hayo yamemfikia mkaguzi wa hesabu.

Uidhinisho wa taarifa ya kifedha

Taarifa ya kifedha inayoonyeshwa katika ukrasa 68 hadi 102 iliidhinishwa kwenye mkutano wa wakurugenzi ulioandaliwa tarehe 15 Februari 2018.

Kwa amri ya halmashauri ya kampuni

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Ruth Ngobi
Katibu wa kampuni

Tarehe: 15 Februari 2018

DIRECTORS' REMUNERATION REPORT

Our Remuneration Policy 2017

The Remuneration Policy and Remuneration Report for the Executive Directors and the Non-Executive Directors, applicable in 2017 were approved by shareholders at the 2017 Annual General Meeting held on 27th April 2017. The Report has been prepared in accordance with the relevant provisions of both the CMA Code of Corporate Governance guidelines on Directors' remuneration, the Kenyan Companies Act, 2015, and reflects the disclosure requirements under IFRS.

Our Principles of Remuneration

The Group and Company's remuneration principles, seek to reward the delivery of the Group's strategy in a simple and straightforward manner, which is aligned to shareholders' long-term sustainable interests. The remuneration structure is designed to recognise the skills and experience of the Directors and ensure it reflects the appropriate reward in a talent competitive market.

Executive Directors

Executive Directors' remuneration comprises of fixed and variable elements. The fixed elements comprise of base salary, pension and other benefits. The variable elements are provided to Executive Directors and Senior Managers via two performance-based incentive schemes; a single cash and share incentive annual bonus plan (IEIS), and a single long-term incentive scheme (LTIP).

We have summarised the key elements below to facilitate the understanding of the Annual Report on Remuneration 2017.

The table below summarises the main elements of the remuneration packages of the Executive Directors as compensation for their role as key management within the BAT Group.

Reward	Purpose and link to strategy	Mechanics of reward	Performance metrics
Basic salary	Attract and retain high calibre individuals to deliver the Company's strategic plans, by offering market competitive remuneration, to reflect an individual's skills and experience.	• Paid in 12 equal monthly instalments during the year and is pensionable; • Reviewed annually with salary changes effective from April, depending on performance.	Individual and business performance.
Pension	Provide competitive post-retirement benefit arrangements so as to attract and retain high calibre talent, to drive delivery of Group's strategy.	• Annual contribution up to 35% of base salary for International Assignees, and 9% of base salary for local staff.	None.
Other benefits	Provide market competitive benefits which: • Facilitate the attraction and retention of high calibre talent to deliver the Group's strategic plans; and • Recognise that such talent is global in source, and that the availability of certain benefits are key enablers for attraction and retention.	Range of benefits include: • Car allowance • Driver and domestic allowance • Medical insurance • Personal life and accident insurance • Security • Education allowances For international assignees additional benefits include: • Travel allowance • Housing allowance • Relocation expense • Tax advice and • Tax equalisation payments	None.
Short term incentives	Incentivise the attainment of corporate targets aligned with the Group's strategic objectives on an annual basis.	• Targets are set annually based on the Group and Company business plans; • Payout is done annually in March after measurements and approval of results; • 60% of the bonus is paid in cash, 40% is awarded as shares in the Parent Company (BAT plc); • Bonus ranges from 0-110% of annual salary for Managing Director, 0-90% for the Finance Director.	• Market share growth (20%); • Volume of global drive brands sold (20%); • Operating profit (40%) and • Cash conversion (20%).
Long term incentives	Incentivise and promote the long-term sustainable success of the Group.	• Targets are set covering a three year period for BAT Group UK results. • The awarded shares in the Parent Company (BAT plc) vest on the third anniversary of the award. • The number of shares that ultimately vest will depend on the extent that the performance conditions, of the BAT Group (UK) have been met, during the three-year performance period.	• Earnings per share(40%); • Total shareholder return (20%); • Net turnover (20%); and • Cash conversion (20%).

Chairman and Non-Executive Directors

The quantum and structure of Non-Executive Directors' remuneration is assessed primarily against the same remuneration comparator group of companies, used for setting the remuneration for Executive Directors.

The table below summarises the elements of reward for Non-Executive Directors.

Reward	Purpose and link to strategy	Mechanics of reward	Performance metrics
Fees	Fees for Non-Executive Directors need to be sufficient to attract, motivate and retain individuals with skills, and senior-level experience to drive the Company's strategy forward.	• Fixed monthly retainer; • Sitting allowance for every committee or board meeting; • Reviewed annually and adjusted as required.	As per Annual Board Evaluation.

Other terms – Non-Executive Directors

Shareholding requirements	• There are no formal requirements for the Non-Executive Directors to hold shares in the Company. However, Non-Executive Directors are encouraged to acquire a small interest during the initial years after their date of appointment; • The Non-Executive Directors do not participate in the British American Tobacco Group share scheme, bonus schemes or incentive plans, and are not members of any Company pension plan.
Terms of appointment	• The Non-Executive Directors do not have service contracts with the Company, but instead have letters of appointment, which are available for inspection at the Company's registered office upon notice.
Terms of termination	• On termination, at any time, a Non-Executive Director is entitled to any accrued but unpaid Director's fees but not to any other compensation.

The Remuneration Committee conducts an annual review to ensure application and alignment of the Policy with the business needs, to promote the long-term success of the Company. There were no substantial changes relating to the Directors' remuneration policy made during the year.

Service Contracts – Executive Directors

Duration of current contracts	The Managing Director has signed a three year contract, while the Finance Director is on a permanent and pensionable contract with the following execution dates:

Executive Director	Execution date
Beverley Spencer-Obatoyinbo	2 May 2017
Sidney Wafula	2 May 2017

Notice period	Thirty (30) days
Provision for early termination of contracts	On early termination of contracts, the Executive Directors are eligible for redundancy packages as follows: • 1 month salary in lieu of notice • 2 months salary • 4 days worth of salary for every month worked In the event that the contract is terminated for cause (such as gross misconduct), the Company may terminate the contract with immediate effect and no compensation would be payable.

Directors' remuneration and compensation as key management for the year ended 31 December 2017

The following table shows a summary of remuneration for the Executive Directors, in respect of qualifying services as directors and compensation as key management, for the year ended 31 December 2017 together with comparative figures for 2016:

Executive Directors	Salary		Taxable benefits		Short-term incentives		Long-term incentives		Pension		Early Retirement		Total	
	KSh.'000		KSh.'000		KSh.'000		KSh.'000		KSh.'000		KSh.'000		KSh.'000	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Beverley Spencer-Obatoyinbo (from 2 May 2017)	12,080	-	8,281	-	4,384	-	12,883	-	-	-	-	-	37,628	-
Keith Gretton (Up-to 1 May 2017)	5,854	15,674	2,785	7,356	-	4,730	6,254	13,531	-	-	-	-	14,893	41,291
Sidney Wafula (from 2 May 2017)	5,833	-	1,961	-	1,888	-	3,316	-	521	-	-	-	13,519	-
Philip Lopokoiyit (Up-to 1 May 2017)	3,449	9,768	1,238	3,451	-	4,173	2,344	6,073	310	913	32,806	-	40,147	24,378
Total remuneration	27,216	25,442	14,265	10,807	6,272	8,903	24,797	19,604	831	913	32,806	-	106,187	65,669

In the year 2017, as part of their compensation, the Executive Directors were awarded shares in the parent company, BAT Group (UK). Beverley Spencer-Obatoyinbo was awarded 2,925 shares and Sidney Wafula was awarded 779 shares. In the prior year 2016, Keith Gretton was awarded 2,760 shares and Philip Lopokoiyit was awarded 1,171 shares. The values of these shares have been included in the table above under Long-term incentives.

The following table shows a summary of remuneration for the Non-Executive Directors, in respect of qualifying services for the year ended 31 December 2017, together with comparative figures for 2016:

Non-Executive Directors	Fixed retainer		Sitting allowance		Chairman honoraria		Total	
	KSh.'000		KSh.'000		KSh.'000		KSh.'000	
Name	2017	2016	2017	2016	2017	2016	2017	2016
George Maina	3,286	3,286	262	242	2,500	2,500	6,048	6,028
Gayling May	1,775	1,775	288	242	-	-	2,063	2,017
Carol Musyoka	1,775	1,775	310	176	-	-	2,085	1,951
Jan Mohamed	1,775	1,775	185	132	-	-	1,960	1,907
Teddy Mapunda	1,775	1,775	166	88	-	-	1,941	1,863
Peter Mwangi	1,775	1,775	191	132	-	-	1,966	1,907
Dr. Martin Oduor-Otieno	1,775	740	263	22	-	-	2,038	762
Jonathan Ciano	-	906	-	44	-	-	-	950
Total remuneration	13,936	13,807	1,665	1,078	2,500	2,500	18,101	17,385

Other required disclosures

Payments to former Directors and payments for loss of office

The Company did not make any payments of money or other assets to former Directors. There were no other sums paid to third parties in respect of Directors' services.

Voting on the Remuneration Report at the 2017 AGM and engagement with shareholders

During the 2017 AGM, held on 27th April 2017, there were no votes cast against, or votes held, with respect to the Directors' remuneration policy and report.

Director's shareholding

Director's shareholding in British American Tobacco Kenya plc as at 15 February 2018 is as follows:

Director	2017	2016
Sidney Wafula	300	-
Carol Musyoka	200	200
Philip Lopokoiyit	-	400

By order of the Board

Ruth Ngobi
Company Secretary

Date: 15 February 2018

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for the preparation and presentation of the financial statements of British American Tobacco Kenya plc, set out on pages 68 to 102, which comprise the consolidated and Company statements of financial position as at 31 December 2017, the consolidated statement of profit or loss and other comprehensive income, consolidated and Company statements of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

The Directors' responsibilities include: determining that the basis of accounting described in Note 2, is an acceptable basis for preparing and presenting the financial statements in the circumstances, preparation and presentation of financial statements in accordance with International Financial Reporting Standards, and in the manner required by the Kenyan Companies Act, 2015, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

Under the Kenyan Companies Act, 2015, the Directors are required to prepare financial statements for each financial year, which give a true and fair view of the financial position of the Group and the Company, as at the end of the financial year, and of the profit or loss of the Group and the Company for that year. It also requires the Directors to ensure the Company and its subsidiaries keep 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 policy supported by reasonable and prudent judgments and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. The Directors are of the opinion that the financial statements give a true and fair view of the financial position of the Group and the Company, and the Group profit or loss and cash flows.

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 Company's and its subsidiaries' ability to continue as a going concern, and have no reason to believe the Company and its subsidiaries 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 15 February 2018.

George Maina	Beverley Spencer-Obatoyinbo	Sidney Wafula
Chairman	Managing Director	Finance Director

Date: 15 February 2018

INDEPENDENT AUDITORS' REPORT
to the members of British American Tobacco Kenya plc

Report on The Audit of The Financial Statements

Opinion

We have audited the financial statements of British American Tobacco Kenya plc and its subsidiaries (the Group) set out on pages 68 to 102, which comprise the consolidated and Company statements of financial position as at 31 December 2017, the consolidated statement of profit or loss and other comprehensive income, consolidated and Company statements of changes in equity, and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give a true and fair view of the consolidated and Company financial position of British American Tobacco Kenya plc at 31 December 2017, and its consolidated financial performance and cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRSs) and the requirements of the Kenyan Companies Act, 2015.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Consolidated and Company Financial Statements section of our report. We are independent of the Group and Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), together with the ethical requirements that are relevant to our audit of the consolidated and Company financial statements in Kenya and, we have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

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

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, we do not provide a separate opinion on these matters.

(a) Provisions and contingent liabilities in respect of litigations

The Group and/the Company is/are subject to claims, which could have an impact on the Group's and/or the Company's results if the potential exposures were to materialise. The Directors apply judgment when considering whether, and how much, to provide for the potential exposure of each litigation. We focused on this area given the complexity and judgment necessary to determine whether to provide for, disclose or not disclose certain exposures.

Our work included, but was not limited to, an assessment of the processes and controls over litigations operated by the Company. We held discussions with the Group's and the Company's in-house legal counsel, including after the year-end, to discuss the nature of on-going claims, and to validate the latest status and accounting and disclosure implications.

We also obtained formal confirmations from the Group's and Company's external counsel for significant litigation matters to ensure completeness of provisioning and disclosure.

We assessed the legal opinion from the external lawyers to challenge the basis used for the provisions recorded or disclosures made by the Company. Where provisions were not required, we also considered the adequacy and completeness of the Group's and the Company's disclosures made in relation to contingent liabilities. These are contained in accounting policy note 3 (i) – Critical accounting estimates and judgments and disclosure note 30 - Contingent liabilities.

Other Information

The Directors are responsible for the other information. The other information comprises the information included in the *Annual Report and Financial Statements*, but does not include the financial statements and our auditors' report thereon.

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

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

Directors' Responsibilities for the Financial Statements

As stated on page 65, the Directors are responsible for the preparation of the financial statements that give a true and fair view in accordance with IFRSs, and in the manner required by the Kenya Companies Act, 2015, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Group's and the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group and/or the Company to cease operations, or have no realistic alternative but to do so. The directors are responsible for overseeing the financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

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

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the consolidated and Company financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit, in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's and the Company's internal control.

- Evaluate the appropriateness of accounting policies used, and the reasonableness of accounting estimates and related disclosures made by the Directors.

- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists, related to events or conditions that may cast significant doubt on the Group's and the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated and Company financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group and/or the Company cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves a fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group, to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

From the matters communicated with the Directors, we determine those matters that were of most significance in the audit of the consolidated and Company financial statements of the current period, and are therefore the key audit matters.

We describe these matters in our auditors' report, unless law or regulation precludes public disclosure about the matter, or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so, would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

As required by the Kenyan Companies Act, 2015 we report to you, based on our audit, that;

i. In our opinion, the information given in the report of the Directors on pages 58 to 61 is consistent with the financial statements;
ii. In our opinion, the auditable part of the Directors' remuneration report on pages 62 to 64 has been properly prepared in accordance with the Kenyan Companies Act, 2015; and
iii. Our report is unqualified.

The Engagement Partner responsible for the audit resulting in this independent auditors' report is FCPA Eric Aholi – P/1471.

KPMG Kenya
8th Floor, ABC Towers
Waiyaki Way
PO Box 40612
00100 Nairobi GPO

Date: 15 February 2018

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

	Notes	Year ended 31 December 2017	2016
		KSh.'000	KSh.'000
Gross revenue		34,467,704	36,676,249
Excise duty and Value Added Tax (VAT)		(15,794,407)	(16,826,348)
Net revenue	5	18,673,297	19,849,901
Raw materials and manufacturing costs	6	(10,731,063)	(10,991,821)
Marketing and distribution costs	7	(1,349,409)	(1,543,866)
Administration and other expenses	8	(1,708,638)	(1,604,839)
Other income		476,823	496,607
Operating profit		5,361,010	6,205,982
Finance costs	9	(494,067)	(294,672)
Profit before tax	10	4,866,943	5,911,310
Income tax expense	12	(1,530,937)	(1,676,976)
Profit for the year		3,336,006	4,234,334
Other comprehensive income			
Items that will not be reclassified to profit or loss - net revaluation surplus		-	616,398
Items that may be reclassified to profit or loss - net fair value gains		7,428	-
Total comprehensive income for the year		3,343,434	4,850,732
Earnings per share:			
Basic and diluted (KSh. per share)	13	33.36	42.34

The notes on pages 76 to 102 are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Notes	Year ended 31 December 2017	2016
		KSh.'000	KSh.'000
Capital and reserves attributable to the Company's equity holders			
Share capital	15	1,000,000	1,000,000
Share premium	15	23	23
Hedging reserve	15	7,428	-
Revaluation surplus	16	1,861,435	1,902,130
Retained earnings		2,721,337	1,944,636
Proposed dividend	14	2,250,000	3,950,000
Total equity		7,840,223	8,796,789
Non-current liabilities			
Borrowings	25	1,239,000	1,229,640
Deferred income tax	17	2,151,722	2,127,411
Total non-current liabilities		3,390,722	3,357,051
Total equity and non-current liabilities		11,230,945	12,153,840
Non-current assets			
Property, plant and equipment	18	9,133,893	9,523,799
Deferred income tax	17	6,443	7,651
		9,140,336	9,531,450
Current assets			
Inventories	20	5,674,768	5,973,456
Receivables and prepayments	21	2,803,043	2,541,910
Derivative financial instruments	22	17,900	-
Current income tax	26	140,668	392,366
Cash and cash equivalents	23	28,873	60,618
		8,665,252	8,968,350
Current liabilities			
Payables and accrued expenses	24	4,757,921	4,540,018
Borrowings	25	1,680,724	1,747,336
Derivative financial instruments	22	7,289	-
Current income tax	26	41,332	-
Provisions for liabilities and charges	27	87,377	58,606
		6,574,643	6,345,960
Net current assets		2,090,609	2,622,390
Total assets		11,230,945	12,153,840

The notes on pages 76 to 102 are an integral part of these financial statements. The financial statements on pages 68 to 102 were approved and authorised for issue by the Board of Directors on 15 February 2018 and signed on its behalf by:

George Maina
Chairman

Beverley Spencer-Obatoyinbo
Managing Director

Sidney Wafula
Finance Director

COMPANY STATEMENT OF FINANCIAL POSITION

	Notes	Year ended 31 December 2017 KSh.'000	2016 KSh.'000
Capital and reserves attributable to the Company's equity holders			
Share capital	15	1,000,000	1,000,000
Share premium	15	23	23
Hedging reserve	15	7,428	-
Revaluation surplus	16	1,861,435	1,902,130
Retained earnings		2,721,337	1,944,636
Proposed dividend		2,250,000	3,950,000
Total equity		7,840,223	8,796,789
Non-current liabilities			
Borrowings	25	1,239,000	1,229,640
Deferred income tax	17	2,149,535	2,127,411
Total non-current liabilities		3,388,535	3,357,051
Total equity and non-current liabilities		11,228,758	12,153,840
Non-current assets			
Property, plant and equipment	18	9,133,893	9,523,799
Investment in subsidiaries	19	12,000	12,000
		9,145,893	9,535,799
Current assets			
Inventories	20	5,633,189	5,953,870
Receivables and prepayments	21	2,834,757	2,418,327
Derivative financial instruments	22	17,900	-
Cash and cash equivalents	23	28,873	55,537
Current income tax	26	-	356,719
		8,514,719	8,784,453
Current liabilities			
Payables and accrued expenses	24	4,615,132	4,360,470
Borrowings	25	1,680,724	1,747,336
Derivative financial instruments	22	7,289	-
Current income tax	26	41,332	-
Provisions for liabilities and charges	27	87,377	58,606
		6,431,854	6,166,412
Net current assets		2,082,865	2,618,041
Total assets		11,228,758	12,153,840

The notes on pages 76 to 102 are an integral part of these financial statements. The financial statements on pages 68 to 102 were approved and authorised for issue by the Board of Directors on 15 February 2018 and signed on its behalf by:

George Maina
Chairman

Beverley Spencer-Obatoyinbo
Managing Director

Sidney Wafula
Finance Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Notes	Share capital	Share premium	Hedging reserve	Revaluation surplus	Retained earnings	Proposed dividends	Total equity
Year ended 31 December 2017		KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000
At start of the year		1,000,000	23	-	1,902,130	1,944,636	3,950,000	8,796,789
Comprehensive income for the year								
Profit for the year		-	-	-	-	3,336,006	-	3,336,006
Transfer of excess depreciation	12	-	-	-	(58,136)	58,136	-	-
Deferred income tax on transfer	12	-	-	-	17,441	(17,441)	-	-
Fair value gain recognised through OCI		-	-	10,611	-	-	-	10,611
Deferred tax in respect of fair value gain		-	-	(3,183)	-	-	-	(3,183)
Net gains recognised directly in equity		-	-	7,428	-	-	-	7,428
Transactions with owners								
Distribution to owners (Dividends) :								
• Final for 2016 paid	14	-	-	-	-	-	(3,950,000)	(3,950,000)
• Interim for 2017 paid	14	-	-	-	-	(350,000)	-	(350,000)
• Proposed final for 2017	14	-	-	-	-	(2,250,000)	2,250,000	-
Total transactions with owners		-	-	-	-	(2,600,000)	(1,700,000)	(4,300,000)
At end of year		1,000,000	23	7,428	1,861,435	2,721,337	2,250,000	7,840,223

The notes on pages 76 to 102 are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (CONTINUED)

	Notes	Share capital	Share premium	Revaluation surplus	Retained earnings	Proposed dividends	Total equity
Year ended 31 December 2016		KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000
At start of the year		1,000,000	23	1,416,219	1,836,936	4,600,000	8,853,178
Comprehensive income for the year							
Profit for the year		-	-	-	4,234,334	-	4,234,334
Gain on revaluation of land and buildings		-	-	876,505	-	-	876,505
Deferred income tax on revaluation	17	-	-	(260,107)	-	-	(260,107)
		-	-	616,398	-	-	616,398
Transfer of excess depreciation	12	-	-	(43,480)	43,480	-	-
Deferred income tax on transfer	12	-	-	13,044	(13,044)	-	-
		-	-	(30,436)	30,436	-	-
Net gains recognised directly in equity		-	-	585,962	30,436	-	616,398
Transfer of revaluation in respect of sale of land and buildings.		-	-	(142,930)	142,930	-	-
Deferred tax on disposed assets		-	-	42,879	-	-	42,879
Transactions with owners							
Distribution to owners (Dividends):							
• Final for 2015 paid	14	-	-	-	-	(4,600,000)	(4,600,000)
• Interim for 2016 paid	14	-	-	-	(350,000)	-	(350,000)
• Proposed final for 2016	14	-	-	-	(3,950,000)	3,950,000	-
Total transactions with owners		-	-	-	(4,300,000)	(650,000)	(4,950,000)
At end of year		1,000,000	23	1,902,130	1,944,636	3,950,000	8,796,789

The notes on pages 76 to 102 are an integral part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY

	Notes	Share capital	Share premium	Hedging reserve	Revaluation surplus	Retained earnings	Proposed dividends	Total equity
Year ended 31 December 2017		KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000
At start of the year		1,000,000	23	-	1,902,130	1,944,636	3,950,000	8,796,789
Comprehensive income for the year								
Profit for the year		-	-	-	-	3,336,006	-	3,336,006
Transfer of excess depreciation	12	-	-	-	(58,136)	58,136	-	-
Deferred income tax on transfer	12	-	-	-	17,441	(17,441)	-	-
Fair value gain recognised through OCI		-	-	10,611	-	-	-	10,611
Deferred tax in respect of fair value gain		-	-	(3,183)	-	-	-	(3,183)
Net gains recognised directly in equity		-	-	7,428	-	-	-	7,428
Transactions with owners								
Distribution to owners (Dividends):								
• Final for 2016 paid	14	-	-	-	-	-	(3,950,000)	(3,950,000)
• Interim for 2017 paid	14	-	-	-	-	(350,000)	-	(350,000)
• Proposed final for 2017	14	-	-	-	-	(2,250,000)	2,250,000	-
Total transactions with owners		-	-	-	-	(2,600,000)	(1,700,000)	(4,300,000)
At end of year		1,000,000	23	7,428	1,861,435	2,721,337	2,250,000	7,840,223

The notes on pages 76 to 102 are an integral part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY (CONTINUED)

	Notes	Share capital	Share premium	Revaluation surplus	Retained earnings	Proposed dividends	Total equity
Year ended 31 December 2016		KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000
At start of year		1,000,000	23	1,416,219	1,836,936	4,600,000	8,853,178
Comprehensive income for the year							
Profit for the year		-	-	-	4,234,334	-	4,234,334
Gain on revaluation of land and buildings		-	-	876,505	-	-	876,505
Deferred income tax on revaluation	17	-	-	(260,107)	-	-	(260,107)
		-	-	616,398	-	-	616,398
Transfer of excess depreciation	12	-	-	(43,480)	43,480	-	-
Deferred income tax on transfer	12	-	-	13,044	(13,044)	-	-
		-	-	(30,436)	30,436	-	-
Net gains recognised directly in equity		-	-	585,962	30,436	-	616,398
Transfer of revaluation in respect of sale of land and buildings.		-	-	(142,930)	142,930	-	-
Deferred tax on disposed assets		-	-	42,879	-	-	42,879
Transactions with owners							
Distribution to owners (Dividends):							
• Final for 2015 paid	14	-	-	-	-	(4,600,000)	(4,600,000)
• Interim for 2016 paid	14	-	-	-	(350,000)	-	(350,000)
• Proposed final for 2016	14	-	-	-	(3,950,000)	3,950,000	-
Total transactions with owners		-	-	-	(4,300,000)	(650,000)	(4,950,000)
At end of year		1,000,000	23	1,902,130	1,944,636	3,950,000	8,796,789

The notes on pages 76 to 102 are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

	Notes	Year ended 31 December 2017	2016
		KSh.'000	KSh.'000
Cash flows from operating activities			
Cash generated from operations	28	6,419,072	7,986,689
Interest received	9	1,798	9,301
Interest paid	9	(491,827)	(324,611)
Income tax paid	26	(1,215,571)	(2,509,944)
Net cash generated from operating activities		4,713,472	5,161,435
Cash flows from investing activities			
Purchase of property, plant and equipment	18	(391,281)	(560,852)
Proceeds from disposal of property, plant and equipment		12,676	274,499
Net cash used in investing activities		(378,605)	(286,353)
Cash flows from financing activities			
Dividends paid to the Company shareholders	14	(4,300,000)	(4,950,000)
Net cash used in financing activities		(4,300,000)	(4,950,000)
Net movement in cash and cash equivalents		34,867	(74,918)
Cash and cash equivalents at beginning of year		(1,686,718)	(1,611,800)
Cash and cash equivalents at end of year	23	(1,651,851)	(1,686,718)

The notes on pages 76 to 102 are an integral part of these financial statements.

NOTES

1. General Information

British American Tobacco Kenya plc is incorporated in Kenya under the Kenyan Companies Act, 2015 as a public limited liability Company, and is domiciled in Kenya. The address of its registered office is:

Likoni Road
P.O Box 30000-00100
Nairobi, Kenya

60% of the Company is controlled by British American Tobacco Plc incorporated in England and Wales, which is also the ultimate parent Company.

The Company's shares are listed on the Nairobi Securities Exchange.

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

2. Summary of significant accounting policies

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

a. Basis of preparation

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

The preparation of financial statements in conformity with IFRSs requires the use of certain critical accounting estimates. It also requires directors to exercise their judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or where assumptions and estimates are significant to the financial statements, are disclosed in Note 3.

New standards and interpretations

i. *New standards, amendments and interpretations effective and adopted during the year*

New standard or amendments

- Disclosure Initiative (Amendments to IAS 7)
- Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12)
- Annual improvements cycle (2014-2016) – (Amendments to IFRS 12 Disclosure of Interest in Other Entities)

Disclosure Initiative (Amendments to IAS 7)

The amendments in the Disclosure Initiative (Amendments to IAS 7) come with the objective that entities shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities.

The International Accounting Standards Board (IASB) requires that the following changes in liabilities arising from financing activities are disclosed (to the extent necessary): (i) changes from financing cash flows; (ii) changes arising from obtaining or losing control of subsidiaries or other businesses; (iii) the effect of changes in foreign exchange rates; (iv) changes in fair values; and (v) other changes.

The IASB defines liabilities arising from financing activities as liabilities "for which cash flows were, or future cash flows will be, classified in the statement of cash flows as cash flows from financing activities". It further stresses that the new disclosure requirements also relate to changes in financial assets if they meet the same definition.

The amendments state that one way to fulfil the new disclosure requirement is to provide a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities.

Finally, the amendments state that changes in liabilities arising from financing activities must be disclosed separately from changes in other assets and liabilities.

The amendments were effective for annual periods beginning on or after 1 January 2017, with early application permitted. The amendments are being issued less than one year before the effective date and hence entities do not need to provide comparative information when they first apply the amendments. The adoption of these changes did not have an impact on the financial statements of the Group since the Group does not have liabilities arising from financing activities.

Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12)

The amendments in Recognition of Deferred Tax Assets for Unrealised Losses clarify the following aspects:

- Unrealised losses on debt instruments measured at fair value and measured at cost for tax purposes give rise to a deductible temporary difference regardless of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use.
- The carrying amount of an asset does not limit the estimation of probable future taxable profits.
- Estimates for future taxable profits exclude tax deductions resulting from the reversal of deductible temporary differences. An entity assesses a deferred tax asset in combination with other deferred tax assets. Where tax law restricts the utilisation of tax losses, an entity would assess a deferred tax asset in combination with other deferred tax assets of the same type.

The amendments were effective for annual periods beginning on or after 1 January 2017 with early application permitted. As transition relief, an entity may recognise the change in the opening equity of the earliest comparative period in opening retained earnings on initial application without allocating the change between opening retained earnings and other components of equity. The Group has not added additional transition relief for first-time adopters.

The adoption of these changes did not have a significant impact on the amounts and disclosures in the financial statements.

Annual improvements cycle (2014-2016) – (Amendments to IFRS 12 Disclosure of Interest in Other Entities)

The disclosure requirements for interests in other entities also apply to interests that are classified as held for sale or distribution. The adoption of these changes did not have an impact on the financial statements of the Group since the Group does not have Interest in Other Entities.

2 Summary of significant accounting policies (continued)

a. Basis of preparation (continued)

ii. New and amended standards and interpretations in issue but not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2017, and have not been early adopted by the Group. The Group is in the process of assessing the impact of these standards on the Company financial statements.

New standards or amendments	Effective for annual periods beginning on or after
• IFRS 9 Financial Instruments (2014)	1 January 2018
• IFRS 15 Revenue from Contracts with Customers	1 January 2018
• Classification and Measurement of Share-based Payment transactions (Amendments to IFRS 2)	1 January 2018
• Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4)	1 January 2018
• IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration	1 January 2018
• Transfers of Investment Property (Amendments to IAS 40)	1 January 2018
• Annual improvements cycle (2014-2016) – (Amendments to IFRS 1 First time adoption of IFRSs and IAS 28 Investments in Associates and Joint Ventures)	1 January 2018
• IFRS 16 Leases	1 January 2019
• IFRIC 23 Income tax exposures	1 January 2019
• Prepayment Features with Negative Compensation (Amendments to IFRS 9)	1 January 2019
• Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)	1 January 2019
• IFRS 17 Insurance Contracts	1 January 2021
• Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS10 and IAS 28)	To be determined

All standards and interpretations will be adopted at their effective date (except for those standards and interpretations that are not applicable to the entity).

IFRS 9: Financial Instruments (2014)

On 24 July 2014, the IASB issued the final IFRS 9 Financial Instruments Standard, which replaces earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement.

This standard introduces changes in the measurement bases of the financial assets to amortised cost, fair value through other comprehensive income or fair value through profit or loss. Even though these measurement categories are similar to IAS 39, the criteria for classification into these categories are significantly different. In addition, the IFRS 9 impairment model has been changed from an "incurred loss" model from IAS 39 to an "expected credit loss" model.

The standard is effective for annual periods beginning on or after 1 January 2018 with retrospective application, early adoption permitted.

The Group and Company are assessing the potential impact on its financial statements resulting from the application of IFRS 9.

IFRS 15 Revenue from Contracts with Customers (Effective 31 December 2018)

This standard replaces IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfer of Assets from Customers and SIC-31 Revenue – Barter of Transactions Involving Advertising Services.

The standard contains a single model that applies to contracts with customers and two approaches to recognising revenue: at a point in time or over time. The standard specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures.

The standard provides a single, principles-based five-step model to be applied to all contracts with customers in recognising revenue being: Identify the contract(s) with a customer; identify the performance obligations in the contract; determine the transaction price; Allocate the transaction price to the performance obligations in the contract; and recognise revenue when (or as) the entity satisfies a performance obligation.

IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group and Company are assessing the potential impact on its financial statements resulting from the application of IFRS 15.

NOTES (continued)

2 Summary of significant accounting policies (continued)

a. Basis of preparation (continued)

ii. *New and amended standards and interpretations in issue but not yet adopted (continued)*

IFRS 16: Leases

On 13 January 2016, the IASB issued IFRS 16 Leases which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The standard defines a lease as a contract that conveys to the customer ('lessee') the right to use an asset for a period of time in exchange for consideration. A Company assesses whether a contract contains a lease on the basis of whether the customer has the right to control the use of an identified asset for a period of time.

The standard eliminates the classification of leases as either operating leases or finance leases for a lessee and introduces a single lessee accounting model.

All leases are treated in a similar way to finance leases. Applying that model significantly affects the accounting and presentation of leases and consequently, the lessee is required to recognise:

i. Assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A Company recognises the present value of the unavoidable lease payments and shows them either as lease assets (right-of-use assets) or together with property, plant and equipment. If lease payments are made over time, a Company also recognises a financial liability representing its obligation to make future lease payments;

ii. Depreciation of lease assets and interest on lease liabilities in profit or loss over the lease term; and

iii. Separate the total amount of cash paid into a principal portion (presented within financing activities) and interest (typically presented within either operating or financing activities) in the statement of cash flows.

IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. However, compared to IAS 17, IFRS 16 requires a lessor to disclose additional information about how it manages the risks related to its residual interest in assets subject to leases.

The standard does not require a Company to recognise assets and liabilities for:

i. Short-term leases (i.e. leases of 12 months or less), and;

ii. Leases of low-value assets

The new Standard is effective for annual periods beginning on or after 1 January 2019. Early application is permitted insofar as the recently issued revenue standard, IFRS 15 Revenue from Contracts with Customers is also applied.

The Group and Company are assessing the potential impact on its financial statements resulting from the application of this standard.

Classification and Measurements of Share-based Payment Transactions (Amendments to IFRS 2)

The following clarifications and amendments are contained in the pronouncement:

- *Accounting for cash-settled share-based payment transactions that include a performance condition*

Up until this point, IFRS 2 contained no guidance on how vesting conditions affect the fair value of liabilities for cash-settled share-based payments. IASB has now added guidance that introduces accounting requirements for cash-settled share-based payments that follows the same approach as used for equity-settled share-based payments.

- *Classification of share-based payment transactions with net settlement features*

IASB has introduced an exception into IFRS 2 so that a share-based payment where the entity settles the share-based payment arrangement net is classified as equity-settled in its entirety provided the share-based payment would have been classified as equity-settled had it not included the net settlement feature.

Accounting for modifications of share-based payment transactions from cash-settled to equity-settled.

Up until this point, IFRS 2 did not specifically address situations where a cash-settled share-based payment changes to an equity-settled share-based payment because of modifications of the terms and conditions. The IASB has introduced the following clarifications:

- On such modifications, the original liability recognised in respect of the cash-settled share-based payment is de-recognised and the equity-settled share-based payment is recognised at the modification date fair value to the extent services have been rendered up to the modification date.

- Any difference between the carrying amount of the liability as at the modification date and the amount recognised in equity at the same date would be recognised in profit and loss immediately.

The amendments are effective for annual periods beginning on or after 1 January 2018. Earlier application is permitted. The amendments are to be applied prospectively. However, retrospective application is allowed if this is possible without the use of hindsight. If an entity applies the amendments retrospectively, it must do so for all of the amendments described above.

The Group and Company are assessing the potential impact on its financial statements resulting from the application of IFRS 2.

Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4)

The amendments in Applying IFRS 9 'Financial Instruments' with IFRS 4 'Insurance Contracts' (Amendments to IFRS 4) provide two options for entities that issue insurance contracts within the scope of IFRS 4:

- An option that permits entities to reclassify, from profit or loss to other comprehensive income, some of the income or expenses arising from designated financial assets; this is the so-called overlay approach;
- An optional temporary exemption from applying IFRS 9 for entities whose predominant activity is issuing contracts within the scope of IFRS 4; this is the so-called deferral approach.

The application of both approaches is optional and an entity is permitted to stop applying them before the new insurance contracts standard is applied.

An entity applies the overlay approach retrospectively to qualifying financial assets when it first applies IFRS 9. Application of the overlay approach requires disclosure of sufficient information to enable users of financial statements to understand how the amount reclassified in the reporting period is calculated and the effect of that reclassification on the financial statements.

An entity applies the deferral approach for annual periods beginning on or after 1 January 2018. Predominance is assessed at the reporting entity level at the annual reporting date that immediately precedes 1 April 2016. Application of the deferral approach needs to be disclosed together with information that enables users of financial statements to understand how the insurer qualified for the temporary exemption

2 Summary of significant accounting policies (continued)

a. Basis of preparation (continued)

ii. *New and amended standards and interpretations in issue but not yet adopted (continued)*

Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4) (continued)

and to compare insurers applying the temporary exemption with entities applying IFRS 9. The deferral can only be made use of for the three years following 1 January 2018. Predominance is only reassessed if there is a change in the entity's activities.

The adoption of these changes is not expected to have a significant impact on the financial statements the Group and Company since they do not issue insurance contracts within the scope of IFRS 4.

IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration

This Interpretation applies to a foreign currency transaction (or part of it) when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognises the related asset, expense or income (or part of it).

This Interpretation stipulates that the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.

This Interpretation does not apply to income taxes, insurance contracts and circumstances when an entity measures the related asset, expense or income on the initial recognition:

a. At fair value; or
b. At the fair value of the consideration paid or received at a date other than the date of initial recognition of the non-monetary asset or non-monetary liability arising from advance consideration (for example, the measurement of goodwill applying IFRS 3 Business Combinations).

The amendments apply retrospectively for annual periods beginning on or after 1 January 2018, with early application permitted.

The adoption of these changes will not have a significant impact on the amounts and disclosures of the financial statements.

IFRIC 23 Clarification on accounting for Income tax exposures

IFRIC 23 clarifies the accounting for income tax treatments that have yet to be accepted by tax authorities, whilst also aiming to enhance transparency.

IFRIC 23 explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.

An uncertain tax treatment is any tax treatment applied by an entity where there is uncertainty over whether that treatment will be accepted by the tax authority.

If an entity concludes that it is probable that the tax authority will accept an uncertain tax treatment that has been taken or is expected to be taken on a tax return, it should determine its accounting for income taxes consistently with that tax treatment. If an entity concludes that it is not probable that the treatment will be accepted, it should reflect the effect of the uncertainty in its income tax accounting in the period in which that determination is made. Uncertainty is reflected in the overall measurement of tax and separate provision is not allowed.

The entity is required to measure the impact of the uncertainty using the method that best predicts the resolution of the uncertainty (that is, the entity should use either the most likely amount method or the expected value method when measuring an uncertainty).

The entity will also need to provide disclosures, under existing disclosure requirements, about

a. Judgments made;
b. Assumptions and other estimates used; and
c. Potential impact of uncertainties not reflected.

The new Standard is effective for annual periods beginning on or after 1 January 2019.

The Group and Company are assessing the potential impact on its financial statements resulting from the application of IFRIC 23.

IFRS 17 Insurance Contracts

IFRS 17 Insurance Contracts sets out the requirements that an entity should apply in reporting information about insurance contracts it issues and reinsurance contracts it holds. An entity shall apply IFRS 17 Insurance Contracts to:

a. Insurance contracts, including reinsurance contracts, it issues;
b. Reinsurance contracts it holds; and
c. Investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts

IFRS 17 requires an entity that issues insurance contracts to report them on the statement of financial position as the total of:

a. The fulfilment cash flows - the current estimates of amounts that the entity expects to collect from premiums and pay out for claims, benefits and expenses, including an adjustment for the timing and risk of those amounts; and
b. The contractual service margin - the expected profit for providing insurance coverage. The expected profit for providing insurance coverage is recognised in profit or loss over time as the insurance coverage is provided.

IFRS 17 requires an entity to recognise profits as it delivers insurance services, rather than when it receives premiums, as well as to provide information about insurance contract profits that the Company expects to recognise in the future. IFRS 17 requires an entity to distinguish between groups of contracts expected to be profit making and groups of contracts expected to be loss-making. Any expected losses arising from loss-making, or onerous, contracts are accounted for in profit or loss as soon as the Company determines that losses are expected. IFRS 17 requires the entity to update the fulfilment cash flows at each reporting date, using current estimates of the amount, timing and uncertainty of cash flows and of discount rates. The entity:

a. Accounts for changes to estimates of future cash flows from one reporting date to another either as an amount in profit or loss or as an adjustment to the expected profit for providing insurance coverage, depending on the type of change and the reason for it; and
b. Chooses where to present the effects of some changes in discount rates—either in profit or loss or in other comprehensive income.

IFRS 17 also requires disclosures to enable users of financial statements to understand the amounts recognised in the entity's statement of financial position and statement of profit or loss and other comprehensive income, and to assess the risks the Company faces from issuing insurance contracts.

IFRS 17 replaces IFRS 4 Insurance Contracts. IFRS 17 is effective for financial periods commencing on or after 1 January 2021. An entity shall apply the standard retrospectively unless impracticable. A Company can choose to apply IFRS 17 before that date, but only if it also applies IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers.

NOTES (continued)

2 Summary of significant accounting policies (continued)

a. Basis of preparation (continued)

ii. *New and amended standards and interpretations in issue but not yet adopted (continued)*

IFRS 17 Insurance Contracts (continued)

The adoption of the standard will not have an impact on the financial statements of the Group and Company since they do not issue insurance contracts within the scope of IFRS 4 or IFRS 9.

Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)

The amendments require the full gain to be recognised when assets transferred between an investor and its associate or joint venture meet the definition of a 'business' under IFRS 3 Business Combinations. Where the assets transferred do not meet the definition of a business, a partial gain to the extent of unrelated investors' interests in the associate or joint venture is recognised. The definition of a business is key to determining the extent of the gain to be recognised.

The effective date for these changes has now been postponed until the completion of a broader review.

The adoption of these changes is not expected to have a significant impact on the financial statements of the Group since the Group does not have any associates or joint ventures.

Transfers of Investment Property (Amendments to IAS 40)

The IASB has amended the requirements in IAS 40 Investment property on when a Company should transfer a property asset to, or from, investment property. A transfer is made when and only when there is an actual change in use – i.e. an asset meets or ceases to meet the definition of investment property and there is evidence of the change in use.

A change in management intention alone does not support a transfer.

The amendments apply for annual periods beginning on or after 1 January 2018. Early adoption is permitted. A Company has a choice on the transition to apply:

- The prospective approach – i.e. apply the amendments to transfers that occur after the date of initial application – and also reassess the classification of property assets held at that date; or
- The retrospective approach – i.e. apply the amendments retrospectively, but only if it does not involve the use of hindsight.

The adoption of these changes is not expected to have a significant impact on the financial statements of the Group and Company since it does not have Investment Property.

Annual improvements cycle (2014-2016) – (Amendments to IFRS 1 First time adoption of IFRSs and IAS 28 Investments in Associates and Joint Ventures)

Standard	Amendments
IFRS 1 First-time Adoption of IFRS	Outdated exemptions for first-time adopters of IFRS are removed effective for annual periods beginning on or after 1 January 2018. The adoption of these changes will not have an impact on the financial statements of the Group since the Group is not a first time adopter of IFRS.
IAS 28 Investments in Associates and Joint Ventures	A venture capital organisation, or other qualifying entity, may elect to measure its investments in an associate or joint venture at fair value through profit or loss. This election can be made on an investment-by-investment basis. A non-investment entity investor may elect to retain the fair value accounting applied by an investment entity associate or investment entity joint venture to its subsidiaries. This election can be made separately for each investment entity associate or joint venture. The adoption of these changes is not expected to have an impact on the financial statements.

Prepayment Features with Negative Compensation (Amendments to IFRS 9)

The amendment removes the word 'additional' so that negative compensation may be regarded as 'reasonable compensation' irrespective of the cause of the early termination. Financial assets with these prepayment features can therefore be measured at amortised cost or at FVOCI if they meet the other relevant requirements of IFRS 9.

The amendment is effective for annual periods beginning on or after 1 January 2019 with early adoption permitted. Retrospective application is required, subject to relevant transitional reliefs. The adoption of these changes is not expected to have a significant impact on the financial statements of the Group and Company since it does not have prepayment features with negative compensation.

2 Summary of significant accounting policies (continued)

a. Basis of preparation (continued)

ii. *New and amended standards and interpretations in issue but not yet adopted (continued)*

Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)

An amendment to IAS 28 Investments in Associates and Joint Ventures will affect companies that finance such entities with preference shares or with loans for which repayment is not expected in the foreseeable future (referred to as long-term interests or 'LTI'). This is common in the extractive and real estate sectors.
The amendment, which addresses equity-accounted loss absorption by LTI, involves the dual application of IAS 28 and IFRS 9 Financial Instruments.

The amendment applies for annual periods beginning on or after 1 January 2019. Early adoption is permitted.

The Group and Company did not early adopt new or amended standards not yet effective in the year ended 31 December 2017.

b. Consolidation

i. *Subsidiaries*

Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred by the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree on an acquisition-by-acquisition basis, either at fair value or at the non-controlling interest's proportionate share of the recognised amounts of acquiree's identifiable net assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying the value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date; any gains or losses arising from such remeasurement are recognised in profit or loss.

Any contingent consideration to be transferred by the Group is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability are recognised in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income.
Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

The excess of the consideration transferred the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If the total of consideration transferred, non-controlling interest recognised and previously held interest measured is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in the income statement

Inter-company transactions, balances, income and expenses on transactions between Group companies are eliminated. Profits and losses resulting from inter-company transactions that are recognised in assets are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group. Investments in subsidiaries are accounted for at cost less impairment. Cost is adjusted to reflect changes in consideration arising from contingent consideration amendments. Cost also includes direct attributable costs of investment.

ii. *Changes in ownership interests in subsidiaries without change of control*

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

iii. *Disposal of subsidiaries*

When the Group ceases to have control, any retained interest in the entity is remeasured to its fair value at the date when control is lost, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities.

This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

c. Functional currency and foreign currency translation

i. *Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Kenya Shillings (KSh.), which is the Group's presentation currency.

ii. *Transactions and balances*

Transactions in foreign currencies during the year are converted into Kenya shillings at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date.

The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss.

d. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Managing Director who makes operational decisions.

NOTES (continued)

2 Summary of significant accounting policies (continued)

e. Revenue recognition

Revenue is measured at fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group and Company's activities. Net revenue is stated net of

value-added tax (VAT), excise duty, returns, rebates and discounts and after eliminating sales within the Group.

The Group and Company recognise revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the Group and Company and when specific criteria have been met for each of the Group and Company's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group and Company base their estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

Revenue is recognised as follows:

i. Sales of goods: The Group manufactures and sells cigarettes to distributors and fellow subsidiaries of the ultimate parent Company. Sales of goods are recognised in the period in which the Group delivers products to the customer, the customer has full discretion over the channel to sell the products and there is no unfulfilled obligation that could affect the customer's acceptance of the goods. Delivery does not occur until the products are shipped to the specified location, the risk of obsolescence and loss has been transferred to the customer and the customer has accepted the products. No element of financing is deemed present as the sales are made with a credit term of 30 days, which is consistent with the market practice.

ii. Sales of services are recognised in the period in which the services are rendered, by reference to completion of the specific transaction assessed on the basis of the actual service provided as a percentage of the total services to be provided.

iii. Royalty income is recognised on an accruals basis in accordance with the substance of the relevant agreements.

iv. Interest income is recognised using the effective interest method.

v. Dividends are recognised as income in the period in which the right to receive payment is established.

f. Property, plant and equipment

All categories of property, plant and equipment are initially recorded at cost. Buildings and land are subsequently shown at fair value, based on periodic, but at least once every five years, valuations by external independent valuers, less subsequent depreciation. All other property, plant, and equipment are stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of land and buildings are credited to other comprehensive income and cumulated in the revaluation surplus reserve in equity. Decreases that offset previous increases of the same asset are charged in other comprehensive income and debited against the revaluation surplus directly in equity; all other decreases are charged to profit or loss. Each year, the difference between depreciation based on the revalued carrying amount of the asset (i.e. the depreciation charged to profit or loss) and the depreciation based on the asset's original cost is transferred from the revaluation surplus to retained earnings.

Depreciation on other assets is calculated using the straight line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

Buildings	2% per annum
Plant and machinery	7% per annum
Vehicles and computers	20% per annum
Furniture, fittings and equipment	10% per annum

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting date.

The carrying amount of the Group's non-current assets is written down immediately to its estimated recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposal of property, plant and equipment are determined by comparing proceeds with the carrying amount and are included in the profit or loss. On disposal of revalued assets, amounts in the revaluation surplus reserve relating to that asset are transferred to retained earnings.

Capital work in progress represents assets that are under construction or that are not immediately available for use, and are not depreciated but are reviewed for impairment.

g. Impairment of non-financial assets

The carrying amounts of the Group's assets, other than deferred tax assets and inventories, are reviewed at each financial 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 inflows that largely are independent from other assets and groups.

Impairment losses are recognised in the 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.

h. Accounting for leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

The Group and Company lease certain property, plant and equipment. Leases of property, plant and equipment where the Group and Company have substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments.

2 Summary of significant accounting policies (continued)

h. Accounting for leases (continued)

Each lease payment is allocated between the liability and finance charges. The corresponding rental obligations, net of finance charges, are included in non-current liabilities. The interest element of the finance charge is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. Property, plant and equipment acquired under finance leases are depreciated over the shorter of the assets useful life and the lease term.

i. Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined by the weighted average method. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity), but excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less the costs of completion and applicable variable selling expenses.

j. Financial assets

i. *Classification*

The Group and Company classify their financial assets in the following categories; at fair value through profit or loss, loans and receivables and available-for-sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the reporting date. These are classified as non-current assets. The Group and Company's loans and receivables comprise 'trade and other receivables' and 'non-current receivables and prepayments' in the statement of financial position.

ii. *Recognition and measurement*

Regular purchases and sales of financial assets are recognised on the trade date, which is the date on which the Group commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Loans and receivables and are carried at amortised cost using the effective interest method.

iii. *Offsetting financial instruments*

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

iv. *Impairment of financial assets*

Assets carried at amortised cost

The Group and Company assess at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation, and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

For loans and receivables category, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in profit or loss. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group and Company may measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in profit or loss.

k. Derivative financial instruments

Derivatives, which comprise solely forward foreign exchange contracts, are initially recognised at fair value on the date the derivative contract is entered into and are subsequently re-measured at their fair value. The derivatives do not qualify for hedge accounting. Changes in the fair value of derivatives are recognised immediately in profit or loss. These derivatives are trading derivatives and are classified as a current asset or liability.

l. Trade receivables

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business.
If the collection is expected in one year or less (or in the normal operating cycle of the business if longer), they are a classified as current assets. If not, they are presented as non-current assets.

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method, less provision for impairment (note j).

m. Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

n. Share capital

Ordinary shares are classified as 'share capital' in equity. Any premium received over and above the par value of the shares is classified as 'share premium' in equity.

NOTES (continued)

2 Summary of significant accounting policies (continued)

o. Cash and cash equivalents

In the statement of cash flows, cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the statement of financial position.

p. Employee benefits

Pension obligations

The Group and Company operate two defined contribution retirement benefit schemes for all their employees. The assets of each scheme are held in separate funds which are administered by an independent fund manager and are funded by contributions from both the Group and employees. The Group's contributions to the schemes are charged to profit or loss in the year to which they relate.

Other entitlements

Employee entitlements to long service awards are recognised when they accrue to employees. The estimated monetary liability for employees' accrued annual leave entitlement at the statement of financial position date is recognised as an expense accrual. The Group and all its employees also contribute to the National Social Security Fund (NSSF), which is a defined contribution scheme.

Termination benefits

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits at the earlier of the following dates: (a) when the Group can no longer withdraw the offer of those benefits; and (b) when the entity recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of termination benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to their present value.

Bonus plans

The Group recognises a liability and an expense for bonuses. The Group recognises a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

q. Current and deferred income tax

The tax expense for the period comprises current and deferred income tax. Tax is recognised in the profit or loss except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill; deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred income tax is determined using tax rates and laws that have been enacted or substantively enacted at the reporting date and are expected to apply when the related deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

r. Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in profit or loss over the period of the borrowings using the effective interest rate method.

Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw-down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalised as a prepayment for liquidity services and amortised over the period of the facility to which it relates.

Borrowings are classified as current liabilities unless there is an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

s. Dividend distribution

Dividends payable to the Company's shareholders are recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders. Proposed dividends are shown as a separate component of equity until declared.

Dividends payable are charged to equity in the period in which they are approved. Proposed dividends are accrued after ratification at a General Meeting of the Company.

t. Provisions

Provisions are recognised when the Group and Company have a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Provisions are not recognised for future operating losses.
Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

u. Borrowing costs

General and specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

2 Summary of significant accounting policies (continued)

v. Related party transactions

The Group discloses the nature, volume and amounts outstanding at the end of each financial year from transactions with related parties, which include transactions with the directors, executive officers and Group or related companies. The related party transactions are at arm's length.

w. Earnings per share and investments in subsidiaries

Earnings per share

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

Investments in subsidiaries

Investments in subsidiaries are carried in the Company's statement of financial position at cost, less provision for impairment losses. Where, in the opinion of the directors', there has been impairment in the value of the investment, the loss is recognised as an expense in the period in which the impairment is identified. On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is charged or credited to profit or loss. Dividends receivable from subsidiaries are recognised as income for the Company in the period in which the right to receive payments is established.

x. Finance income and finance costs

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets and changes in the fair value of financial assets at fair value through profit or loss. Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date that the Group's right to receive payment is established, which in the case of quoted securities is the ex-dividend date.

Finance costs comprise interest expense on borrowings, unwinding of the discount on provisions, changes in the fair value of financial assets at fair value through profit or loss, impairment losses recognised on financial assets. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.
Foreign currency gains and losses are reported on a net basis

y. Comparatives

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

3. Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including experience of future events that are believed to be reasonable under the circumstances. The Group and Company make estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

i. *Provisions and contingent liabilities*

The Group has provisions which are set up in the ordinary course of business and are related to general liabilities to various stakeholders. The Group follows the guidance of IAS 37 to determine whether a provision is required.

ii. *Useful lives of property plant and equipment*

Property plant and equipment are depreciated over their useful lives. The actual lives of the assets are assessed annually and may vary depending on a number of factors. Management applies judgement in determining useful lives.

iii. *Income taxes*

The Company is subject to income taxes in Kenya. Significant judgment is required in determining the Company's provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Company recognises liabilities on the basis of amounts expected to be paid to the tax authorities. Where the final tax outcome is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

4. Financial risk management

The Group and Company's activities expose them to a variety of financial risks, market risk (including currency and interest risk), credit risk and liquidity risk. The Group and Company's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on its financial performance.

Risk management is carried out by the management under policies approved by the Board of Directors. Management identifies and evaluates financial risks where applicable. The Board provides written principles for overall risk management, as well as written policies covering specific areas such as foreign exchange risk, interest rate risk, credit risk, use of derivative and non-derivative financial instruments and investing excess liquidity.

a. Market risk

i. *Foreign exchange risk*

The Group and Company operate internationally and are exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar, British Pound and Euro. Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities that are denominated in a currency that is not the entity's functional currency. The Group manages foreign exchange risk arising from future commercial transactions and recognised assets and liabilities by regularly revising prices and robust working capital management.

NOTES (continued)

4. Financial risk management (continued)

a. Market risk (continued)

i. Foreign exchange risk (continued)

Below is a summary of the Group and Company's exposure to currency risk at their carrying amounts in Kenya shillings equivalent:

	USD	GBP	EUR
	KSh.'000	KSh.'000	KSh.'000
31 December 2017			
Asset			
Receivables and prepayments	500,870	-	13,664
Cash and cash equivalents	1,404	2,457	222
	502,274	2,457	13,886
Liabilities			
Payables and accrued expenses	1,452,910	89,770	63,885
Borrowings	1,239,000	-	-
	2,691,910	89,770	63,885
31 December 2016			
Asset			
Receivables and prepayments	719,384	138,496	78,166
Cash and cash equivalents	3,176	8,614	13,954
	722,560	147,110	92,120
Liabilities			
Payables and accrued expenses	164,987	-	-
Borrowings	1,229,640	-	-
	1,394,627	-	-

The following are the exchange rates that existed at the financial year end for the following significant currencies:

	USD	GBP	EUR
2017			
Average rates	103.41	133.27	116.82
Closing rates	103.23	138.75	123.28
2016			
Average rates	101.51	137.51	112.33
Closing rates	102.47	126.62	108.08

The following sensitivity analysis shows how profit or loss and equity would change if the market risk variables had been different at the reporting period with all other variables held constant.

	2017	2016
	KSh.'000	KSh.'000
Currency – USD		
10% movement effect (higher/lower)	218,964	67,207
Currency – GBP		
10% movement effect (higher/lower)	8,731	14,711
Currency – EUR		
10% movement effect (higher/lower)	5,000	9,212

4. Financial risk management (continued)

a. Market risk (continued)

i. Foreign exchange risk (continued)

The following table shows the maturity periods for the cash flows associated with derivative financial instruments and the expected impact to profit or loss on undiscounted contractual basis. These relate to the derivative financial instruments as disclosed under note 22.

Forward foreign currency contracts	2017			2016		
	Assets	Liabilities	Total	Assets	Liabilities	Total
	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Carrying amounts	17,900	(7,289)	10,611	-	-	-
Expected cash flows:						
1-6 months	37,964	-	37,964	-	-	-
6-12 months	43,055	29,343	72,398	-	-	-
More than 1 year	-	-	-	-	-	-
Total	81,019	29,343	110,362	-	-	-

ii. Price risk

The Group and the Company are not exposed to equity securities price risk.

iii. Cash flow and fair value interest rate risk

The Group and Company's interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the Group and Company to cash flow interest rate risk which is partially offset by cash held at variable rates. The Group and Company regularly monitor financing options available to ensure optimum interest rates are obtained. At 31 December 2017, an increase/decrease of 1% would have resulted in a change of KSh. 12,409,200 (2016: KSh. 12,397,829) in Group and Company post-tax profit.

b. Credit risk

Credit risk is managed on a Group basis. Credit risk arises from deposits with banks, as well as trade and other receivables. Neither the Group nor the Company has any significant concentrations of credit risk. Credit risk is the risk that a counter-party will default on its contractual obligations resulting in financial loss to the Group and Company.

For banks and financial institutions, only reputable well established financial institutions are accepted. For trade receivables, Group management assesses the credit quality of each customer, taking into account its financial position, past experience and other factors. The utilisation of credit limits is regularly monitored. No credit limits were exceeded during the reporting period, and management does not expect any losses from non-performance by these counter-parties.

The amount that best represents the Group and Company's maximum exposure to credit risk at 31 December 2017 and 31 December 2016 is made up as follows:

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Cash and cash equivalents	28,873	60,618	28,873	55,537
Amounts due from related parties	677,444	1,249,633	677,444	1,247,755
Trade and other receivables	1,734,782	1,239,033	753,940	1,121,544
Derivative financial instruments	17,900	-	17,900	-
	2,458,999	2,549,284	1,478,157	2,424,836

No collateral is held for any of the above assets. All receivables that are neither past due nor impaired are within their approved credit limits, and no receivables have had their terms renegotiated. None of the above assets are either past due or impaired.

c. Liquidity risk

Liquidity risk is the risk that the Group and Company will not be able to meet their financial obligations as they fall due. Prudent liquidity risk management includes maintaining sufficient cash, and the availability of funding from an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, the treasury department maintains flexibility in funding by maintaining availability under committed credit lines.

NOTES (continued)

4. Financial risk management (continued)

c. Liquidity (continued)

Management perform cash flow forecasting and monitor rolling forecasts of the Group and Company's liquidity requirements to ensure it has sufficient cash to meet its operational needs while maintaining sufficient headroom on its undrawn committed borrowing facilities (Note 25) at all times so that the Group and Company do not breach borrowing limits or covenants (where applicable) on any of their borrowing facilities.

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

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

i. Group	Less than 1 year	Between 1 & 4 years
	KSh.'000	KSh.'000
At 31 December 2017		
Liabilities		
Borrowings	1,680,724	1,433,586
Trade and other payables	3,226,554	-
Amounts due to related parties	173,971	-
Derivative financial instruments	7,289	-
Total financial liabilities	5,088,538	1,433,586
Assets		
Cash and bank balances	28,873	-
Amounts due from related parties	677,444	-
Trade and other receivables	1,734,782	-
Derivative financial instruments	17,900	
Total financial assets	2,458,999	-
At 31 December 2016		
Liabilities		
Borrowings	1,747,336	1,378,562
Trade and other payables	3,351,339	-
Amounts due to related parties	190,416	-
Total financial liabilities	5,289,091	1,378,562
Assets		
Cash and bank balances	60,618	-
Amounts due from related parties	1,249,633	-
Trade and other receivables	1,239,033	-
Total financial liabilities	2,549,284	-

4. Financial risk management (continued)

c. Liquidity (continued)

ii. Company	Less than 1 year	Between 1 & 4 years
	KSh.'000	KSh.'000
At 31 December 2017		
Liabilities		
Borrowings	1,680,724	1,433,586
Trade and other payables	3,100,691	-
Amounts due to related parties	157,047	-
Derivative financial instruments	7,289	-
Total financial liabilities	4,945,751	1,433,586
Assets		
Cash and bank balances	28,873	-
Amounts due from related parties	1,999,133	-
Trade and other receivables	753,940	-
Derivative financial instruments	17,900	-
Total financial assets	2,799,846	-
At 31 December 2016		
Liabilities		
Borrowings	1,747,336	1,378,562
Trade and other payables	2,948,705	-
Amounts due to related parties	159,752	-
Total financial liabilities	4,855,793	1,378,562
Assets		
Cash and bank balances	55,537	-
Amounts due from related parties	1,247,755	-
Trade and other receivables	1,121,544	-
Total financial assets	2,424,836	-

For both Group and Company, there are no financial assets or liabilities older than 4 years.

d. Capital risk management

Capital comprises all components of equity as shown in the statement of changes in equity plus net debt. The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, issue new capital or sell assets to reduce debt.

NOTES (continued)

4. Financial risk management (continued)

d. Capital risk management (continued)

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings less cash and cash equivalents. Total capital is calculated as equity plus net debt.

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Total borrowings	2,919,724	2,976,976	2,919,724	2,976,976
Less: cash and cash equivalents	(28,873)	(60,618)	(28,873)	(55,537)
Net debt	2,890,851	2,916,358	2,890,851	2,921,439
Total equity	7,816,110	8,796,789	7,816,110	8,796,789
Total capital	10,706,961	11,713,147	10,706,961	11,718,228
Gearing ratio	27%	25%	27%	25%

Financial instruments by category

Financial assets:

All of the Group and Company's financial assets are classified as loans and receivables and comprise:

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Trade and other receivables (excluding pre-payments)	2,569,592	2,488,666	2,746,668	2,369,299
Cash and cash equivalents	28,873	60,618	28,873	55,537
Derivative financial instruments	17,900	-	17,900	-
	2,616,365	2,549,284	2,793,441	2,424,836

Financial liabilities:

All of the Group and Company's financial liabilities are classified as liabilities at amortised cost and comprise:

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Trade and other payables (excluding statutory liabilities)	3,400,525	3,541,755	3,257,738	3,108,457
Borrowings	2,919,724	2,976,976	2,919,724	2,976,976
Derivative financial instruments	7,289	-	7,289	-
	6,327,538	6,518,731	6,184,751	6,085,433

e. Fair value

A number of the Group's accounting policies and disclosures require the determination of fair values, for both financial and non-financial assets and liabilities.

Below is the fair value measurements disclosure using a three-level fair value hierarchy that reflects the significance of the inputs used in determining the measurements. It should be noted that these disclosures only cover instruments measured at fair value.

4. Financial risk management (continued)

e. Fair value (continued)

Level 1

Included in Level 1 category are financial assets and liabilities that are measured in whole or in part by reference to published quotes in an active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Level 2

Included in Level 2 category are financial assets and liabilities measured using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). For example, instruments measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions are categorised as Level 2. Financial assets and liabilities measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions are assets and liabilities for which pricing is obtained via pricing services, but where prices have not been determined in an active market, financial assets with fair values based on broker quotes, investments in private equity funds with fair values obtained via fund managers and assets that are valued using the Group's own models whereby the majority of assumptions are market observable.

Level 3

Financial assets and liabilities measured using inputs that are not based on observable market data are categorised as Level 3. Non-market observable inputs means that fair values are determined in whole or in part using a valuation technique (model) based on assumptions that are neither supported by prices from observable current market transactions in the same instrument nor are they based on available market data. Valuation techniques are used to the extent that observable inputs are not available, thereby allowing for situations for which there is little, if any, market activity for the asset or liability at the measurement date.

However, the fair value measurement objective remains the same, that is, an exit price from the perspective of the Group. Therefore, unobservable inputs reflect the Group's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). These inputs are developed based on the best information available, which might include the Group's own data. However, significant portion of the unquoted shares have been valued at cost and variation in inputs would not have significant fair value change.

The following table shows an analysis of non-financial assets held at fair value as at 31 December 2017 and 31 December 2016 (Note 18):

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Property, plant and equipment	9,133,893	9,523,799	9,133,893	9,523,799
Total assets	9,133,893	9,523,799	9,133,893	9,523,799

5. Segment information

The Managing Director is the Group's chief operating decision-maker. The Managing Director considers the business from a geographic and product perspective. Geographically, management considers the performance in Local Sales and Export Sales. From a product perspective, management considers sales of cigarettes and cut rag (semi-processed tobacco). All the products are manufactured through the same process and in the same location. The group is considered as one reportable operating segment.

	2017	2016
Analysis of net revenue by geography:	KSh.'000	KSh.'000
Local sales	9,518,057	11,046,135
Export sales	9,155,240	8,803,766
	18,673,297	19,849,901
Analysis of net revenue by product:		
Sale of cigarettes	18,059,817	18,963,855
Sale of cut rag	613,480	886,046
	18,673,297	19,849,901

6. Raw materials and manufacturing costs

	2017	2016
Raw materials, consumables and other manufacturing costs*	10,106,590	10,384,136
Depreciation of property, plant and equipment	624,473	607,685
	10,731,063	10,991,821

*Raw materials, consumables and other manufacturing costs include employee expenses of KSh. 1,198,942,357 (2016: KSh. 1,130,980,351)

NOTES (continued)

	2017	2016
	KSh.'000	KSh.'000
7. Marketing and distribution costs		
Employment expenses	414,697	398,091
Freight and other expenses	934,712	1,145,775
	1,349,409	1,543,866
8. Administration and other expenses		
Employment expenses	566,117	531,559
Recharges and other expenses	750,999	735,120
Reorganisation costs	391,522	338,160
	1,708,638	1,604,839
9. Finance costs		
Interest income	(1,798)	(9,301)
Interest expense	491,827	324,611
Net foreign currency exchange losses/(gains)	4,038	(20,638)
	494,067	294,672
10. Profit before tax		
The following items have been charged in arriving at the profit before income tax:		
Employee benefits expense (Note 11)	2,571,278	2,398,790
Auditors' remuneration	9,740	9,740
Depreciation (Note 18)	780,591	759,606
Profit on sale of property, plant and equipment	(12,080)	(32,624)
11. Employee benefits expense		
Salaries and wages	2,081,691	1,971,319
Retirement benefits costs:		
• Defined contribution scheme	95,907	86,736
• National Social Security Fund	2,158	2,575
Reorganisation costs (Note 8)	391,522	338,160
	2,571,278	2,398,790
12. Income tax		
Current income tax		
Current tax on profits for the year	1,508,601	1,760,091
Total current tax	1,508,601	1,760,091
Deferred income tax (Note 17)		
• Deferred income tax	(326)	(76,593)
• Prior year under/(over) provision of deferred tax	22,662	(6,522)
Total deferred income tax	22,336	(83,115)
Income tax expense	1,530,937	1,676,976

12. Income tax (continued)

The tax (charge)/credit relating to components of equity are as follows:

	2017 KSh.'000			2016 KSh.'000		
	Before tax	Tax charge	After tax	Before tax	Tax charge	After tax
Transfer of excess depreciation	58,136	(17,441)	40,695	43,480	(13,044)	30,436

13. Earnings per share

Basic earnings per share are calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

	2017	2016
	KSh.'000	KSh.'000
Profit attributable to equity holders of the Company (KSh. '000)	3,336,006	4,234,334
Weighted average number of ordinary shares in issue (thousands)	100,000	100,000
Basic earnings per share (KSh.)	33.36	42.34

14. Dividends per share

During the year a final dividend in respect of the 2016 financial results of KSh. 39.50 (2015: KSh. 46.00) and an interim dividend of KSh. 3.50 per share (2015: KSh. 3.50) was declared and paid. The total dividend paid in the year is therefore KSh. 43.00 per share (2015: KSh. 49.50), amounting to a total of KSh. 4,300,000,000 (2016: KSh. 4,950,000,000).

At the annual general meeting to be held on 11 May 2018, a final dividend in respect of the year ended 31 December 2017 of KSh. 22.50 per share amounting to a total of KSh. 2,250,000,000 is to be proposed. These financial statements do not reflect this dividend as a liability.

Payment of dividends is subject to withholding tax at a rate of either 5% or 10% depending on the residence of the respective shareholders.

15. Capital and reserves

i. Share capital – Group and Company

	Number of shares	Ordinary shares	Share premium
	(Thousands)	KSh.'000	KSh.'000
Authorised, issued and fully paid			
Balance at beginning and end of year	100,000	1,000,000	23

The total authorised number of ordinary shares is 100,000,000 with a par value of KSh. 10 per share. All issued shares are fully paid. All shares rank equally with regard to the Company's residual assets. The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

ii. Share premium

Share premium arose when the shares of the Company were issued at a price higher than the par value.

iii. Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of hedging instruments pending subsequent recognition in profit or loss as the hedged items affect profit or loss.

16. Revaluation surplus

The revaluation reserve surplus relates to the revaluation of the Group and Company's land and buildings net of deferred income tax and is non-distributable. The movements in the revaluation surplus are set out in the Group and Company statements of changes in equity.

NOTES (continued)

17. Deferred income tax

	2017	2016
	KSh.'000	KSh.'000
The analysis of Group deferred tax assets and deferred liabilities is as follows		
Deferred tax assets	(6,443)	(7,651)
Deferred tax liabilities	2,151,722	2,127,411
Deferred tax liabilities (net)	2,145,279	2,119,760

Deferred income tax is calculated using the enacted income tax rate of 30% (2016:30%). The movement on the Group deferred income tax account is as follows:

	2017	2016
	KSh.'000	KSh.'000
At start of year	2,119,760	1,985,647
Charge to statement of profit or loss and other comprehensive income	(326)	(76,593)
Prior year under/(over) provision of deferred tax	22,662	(6,522)
Credit to equity	3,183	260,107
Deferred tax on disposal of revalued assets	-	(42,879)
At end of year	2,145,279	2,119,760

Consolidated Group deferred tax assets and liabilities and deferred income tax charge in the consolidated income statement are attributable to the following items.

	1.1.2017	Charged /(credited) to P&L	Charged /(credited) to equity	31.12.2017
Year ended 31 December 2017	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Deferred income tax liabilities				
Property, plant and equipment:				
• On historical cost basis	1,539,851	(80,073)	-	1,459,778
• On revaluation surpluses	774,821	20,549	-	795,370
• On disposal of assets	(42,879)	42,879	-	-
Unrealised exchange gains	110,741	(101,969)	-	8,772
Deferred tax in respect of fair value gain on hedge reserve	-	-	5,370	5,370
	2,382,534	(118,614)	5,370	2,269,290
Deferred income tax assets				
Provisions for liabilities and charges	(137,885)	25,432	-	(112,453)
Unrealised exchange losses	(124,889)	115,518	-	(9,371)
Deferred tax in respect of fair value loss on hedge reserve	-	-	(2,187)	(2,187)
	(262,774)	140,950	(2,187)	(124,011)
Net deferred income tax liability	2,119,760	22,336	3,183	2,145,279

17. Deferred income tax (continued)

	1.1.2016	Charged/ (credited) to P&L	Charged/ (credited) to equity	31.12.2016
Year ended 31 December 2016	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Deferred income tax liabilities				
Property, plant and equipment:				
• On historical cost basis	1,653,769	(113,918)	-	1,539,851
• On revaluation surpluses	514,714	-	260,107	774,821
• On disposal of assets	-	-	(42,879)	(42,879)
Unrealised exchange gains	85,075	25,666	-	110,741
	2,253,558	(88,252)	217,228	2,382,534
Deferred income tax assets				
Provisions for liabilities and charges	(156,994)	19,109	-	(137,885)
Unrealised exchange losses	(110,917)	(13,972)	-	(124,889)
	(267,911)	5,137	-	(262,774)
Net deferred income tax liability	1,985,647	(83,115)	217,228	2,119,760

Deferred income tax of KSh. 17,441,000 (2016: 13,044,000) was transferred within shareholders' equity from revaluation reserves to retained earnings. This represents deferred income tax on the difference between the actual depreciation on the property and the equivalent depreciation based on the historical cost of the property.

Company deferred income tax assets and liabilities are attributable to the following items:

	2017	2016
	KSh.'000	KSh.'000
The analysis of Company deferred tax assets and deferred liabilities is as follows		
Deferred tax liabilities (net)	2,149,535	2,127,411
Deferred income tax liabilities		
Property, plant and equipment:		
• On historical cost basis	1,459,778	1,533,608
• On revaluation surpluses	795,370	774,686
• On disposal of assets	-	(42,879)
Deferred tax in respect of fair value gain on hedge reserve	5,370	-
Unrealised exchange gains	8,772	(71,875)
Total deferred income tax liabilities	2,269,290	2,193,540
Deferred income tax assets		
Provisions for liabilities and charges	(108,197)	(137,171)
Unrealised exchange losses	(9,371)	71,042
Deferred tax in respect of fair value loss on hedge reserve	(2,187)	-
Total deferred income tax assets	(119,755)	(66,129)
Net deferred income tax liability	2,149,535	2,127,411

NOTES (continued)

18. Property, plant and equipment – Group and Company

	Land and Buildings	Plant and Machinery	Vehicles and Equipment	Construction in Progress*	Total
	KSh.'000	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Year ended 31 December 2017					
Opening net book amount	3,944,211	4,950,730	229,382	399,476	9,523,799
Additions	10,636	183,392	36,128	161,125	391,281
Disposals					
• Cost	-	(13,658)	(40,806)	-	(54,464)
• Accumulated depreciation	-	13,250	40,618	-	53,868
Depreciation charge	(89,310)	(594,715)	(96,566)	-	(780,591)
Transfers	-	300,378	4,151	(304,529)	-
Closing net book amount	3,865,537	4,839,377	172,907	256,072	9,133,893
At 31 December 2017					
Cost or valuation	5,002,993	10,060,883	1,146,640	256,072	16,466,588
Accumulated depreciation	(1,137,456)	(5,221,506)	(973,733)	-	(7,332,695)
Net book amount	3,865,537	4,839,377	172,907	256,072	9,133,893
Year ended 31 December 2016					
Opening net book amount	3,303,272	5,159,213	257,218	368,220	9,087,923
Additions	17,081	341,465	93,591	108,715	560,852
Revaluation	876,505	-	-	-	876,505
Disposals					
• Cost	(216,826)	(210,910)	(120,822)	-	(548,558)
• Accumulated depreciation	25,615	165,020	116,048	-	306,683
Depreciation charge	(74,587)	(567,166)	(117,853)	-	(759,606)
Transfers	13,151	63,108	1,200	(77,459)	-
Closing net book amount	3,944,211	4,950,730	229,382	399,476	9,523,799
At 31 December 2016					
Cost or valuation	4,992,357	9,590,771	1,147,167	399,476	16,129,771
Accumulated depreciation	(1,048,146)	(4,640,041)	(917,785)	-	(6,605,972)
Net book amount	3,944,211	4,950,730	229,382	399,476	9,523,799

*Construction in progress relates to factory building under construction and plant and machinery under installation at year end

In 2016, Knight Frank Valuers Limited, professionally valued the Group's land and buildings. The valuation was on an open market value basis. The valuer used the Comparables method of valuation for valuation of land. This is defined as a set of procedures in which a valuer derives the value by comparing the property being valued to similar properties that have recently been sold applying appropriate units of comparison and making adjustments to the sale prices of the comparable sales.

The technique is based on the principal of substitution which states that 'the value of a property tends to be set by the price that would be paid to acquire a substitute property of similar utility and desirability within a reasonable amount of time. Buildings were valued on the basis of Depreciated Replacement Cost (Private Sector) which is defined as the Current Gross Replacement Cost of the improvements, less allowance for physical deterioration and all relevant forms of obsolescence and optimisation.

18. Property, plant and equipment – Group and Company (continued)

The fair value measurement of revalued items of property plant and equipment has been categorised as a level 3 fair value based on the inputs to the valuation techniques.

If the land and buildings were stated on the historical cost basis, the amounts would be as follows:

	2017	2016
	KSh.'000	KSh.'000
Cost	1,654,346	1,643,710
Accumulated depreciation	(444,653)	(355,343)
Net book amount	1,209,693	1,288,367

There are no assets that have been pledged as collateral for loans.
There was no impairment of property, plant and equipment during the year.

19. Investment in subsidiaries

The Company's interest in its subsidiaries, all of which are wholly owned, incorporated in Kenya, unlisted and have the same year end as the Company, were as follows:

Subsidiary	Principal activity	Cost
		KSh.'000
BAT Kenya Tobacco Company Limited	Selling of cigarettes	12,000
African Cigarette Company (Overseas) Limited	Dormant	-
East Africa Tobacco Company (Kenya) Limited	Dormant	-
	Totals	12,000

20. Inventories

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Raw materials and consumables	5,165,105	5,403,667	5,165,105	5,403,667
Finished goods	509,663	569,789	468,084	550,203
	5,674,768	5,973,456	5,633,189	5,953,870

21. Receivables and prepayments

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Trade receivables	1,033,830	635,815	52,244	-
Other receivables	858,318	603,218	701,696	1,121,544
Prepayments	233,451	53,244	81,684	49,028
Due from related parties	677,444	1,249,633	1,999,133	1,247,755
	2,803,043	2,541,910	2,834,757	2,418,327

The carrying amounts of the above receivables and prepayments approximate to their fair values.

NOTES (continued)

22. Derivative financial instruments – Group and Company

The fair values of derivatives are determined based on market data (primarily yield curves, implied volatilities and exchange rates) to calculate the present value of all estimated flows associated with each derivative at the balance sheet date. In the absence of sufficient market data, fair values is based on the quoted market price of similar derivatives.

	Group and Company			
	2017		2016	
	Assets	Liabilities	Assets	Liabilities
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Forward foreign currency contracts	17,900	7,289	-	-
Current	17,900	7,289	-	-
Non-current	-	-	-	-
	17,900	7,289	-	-

These derivatives principally consist of forward foreign currency contracts which have been designated as hedges due to their value changes offsetting with other components of net finance costs relating to financial assets and financial liabilities. The Group does not use derivatives for speculative purposes. All derivatives are undertaken for risk management purposes.

23. Cash and cash equivalents

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Cash at bank	28,873	60,618	28,873	55,537

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise the following:

	Group	
	2017	2016
	KSh.'000	KSh.'000
Cash at bank	28,873	60,618
Bank overdrafts (Note 25)	(1,680,724)	(1,747,336)
	(1,651,851)	(1,686,718)

24. Payables and accrued expenses

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Trade payables	2,166,104	901,829	2,098,687	850,874
Due to related companies	173,971	190,416	157,047	159,752
Other payables and accrued expenses	2,417,846	3,447,773	2,359,398	3,349,844
	4,757,921	4,540,018	4,615,132	4,360,470

25. Borrowings

	Group		Company	
Non-current	2017	2016	2017	2016
Loan from BATIF	1,239,000	1,229,640	1,239,000	1,229,640
Current				
Bank overdrafts	1,680,724	1,747,336	1,680,724	1,747,336
	2,919,724	2,976,976	2,919,724	2,976,976

The loan from BATIF is an unsecured US Dollar denominated floating rate loan repayable by 31 July 2021 at an interest rate of USD LIBOR plus 4.675% up to 28 September 2017. The floating interest rate changed to USD LIBOR plus 2.00% on 29 September 2017 for the remaining period to 31 July 2021. The carrying amounts of short-term borrowings approximate to their fair value. None of the borrowings were in default at any time during the year.

The Group and Company have the following undrawn borrowing facilities:
The facilities are open ended. Bond guarantees are issued in favour of the Kenya Revenue Authority to cover import duty and excise payable.

	2017	2016
	KSh.'000	KSh.'000
Overdraft facilities	6,097,716	4,948,535
Bond guarantees	453,336	1,035,411
	6,551,052	5,983,946

26. Current tax movement

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Opening income tax asset	392,366	(357,487)	356,719	(439,402)
Charge to statement of profit or loss and other comprehensive income	(1,508,601)	(1,760,091)	(528,759)	(411,379)
Income tax paid	1,215,571	2,509,944	130,708	1,207,500
Closing income tax asset/(liability)	99,336	392,366	(41,332)	356,719
Current asset	140,668	392,366	-	356,179
Current liability	(41,332)	-	(41,332)	-
Closing income tax asset/(liability)	99,336	392,366	(41,332)	356,179

NOTES (continued)

27. Provisions for liabilities and charges

	Group	Company
	KSh.'000	KSh.'000
Year ended 31 December 2017		
At start of year	58,606	58,606
Additional provisions	38,923	38,923
Unused amounts reversed	(10,152)	(10,152)
Charge to statement of profit or loss and other comprehensive income	28,771	28,771
At end of year	87,377	87,377
Year ended 31 December 2016		
At start of year	121,490	121,490
Additional provisions	-	-
Unused amounts reversed	(57,618)	(57,618)
Credit to statement of profit or loss and other comprehensive income	(57,618)	(57,618)
Utilised during the year	(5,266)	(5,266)
At end of year	58,606	58,606

Provisions comprise balances set up in the ordinary course of business and are related to general liabilities to various stakeholders.

28. Cash generated from operations

	2017	2016
	KSh.'000	KSh.'000
Profit before taxation	4,866,943	5,911,310
Adjustments for:		
Depreciation (Note 18)	780,591	759,606
Profit on sale of property, plant and equipment	(12,080)	(32,624)
Interest received (Note 9)	(1,798)	(9,301)
Interest expense (Note 9)	491,827	324,611
Unrealised foreign exchange losses	9,360	2,040
Changes in working capital:		
• Inventories	298,688	981,218
• Receivables and prepayments	(261,133)	(42,985)
• Payables and accrued expenses	217,903	155,698
• Provisions for liabilities and charges	28,771	(62,884)
Cash generated from operations	6,419,072	7,986,689

29. Related party transactions

The Group is controlled by British American Tobacco Plc incorporated in England and Wales, which is also the ultimate parent of the Group. There are other companies that are related to British American Tobacco Kenya plc through common shareholdings or common directorships.

The Company has an operating subsidiary, BAT Kenya Tobacco Company Limited.
The following transactions were carried out with related parties.

	Group		Company	
	2017	2016	2017	2016
	KSh.'000	KSh.'000	KSh.'000	KSh.'000
i) Sale of goods and services				
Subsidiary	-	-	18,656,394	17,622,096
Other related parties	7,124,808	7,161,785	7,124,808	7,161,785
	7,124,808	7,161,785	25,781,202	24,783,881
ii) Purchase of goods and services				
Parent Company	308,768	337,512	308,768	337,512
Other related parties	992,929	939,710	992,929	939,710
	1,301,697	1,277,222	1,301,697	1,277,222
iii) Outstanding balances arising from sale and purchase of goods/services				
Receivables from other related parties	677,444	1,249,633	1,999,133	1,247,755
Payables to the Parent Company	38,512	7,747	38,512	7,747
Payables to other related parties	135,459	182,669	118,535	152,005
	173,971	190,416	157,047	159,752

The amounts outstanding are unsecured and will be settled in cash. No interest is charged on outstanding balances and no guarantees have been given or received.

	Group		Company	
	2017	2016	2017	2016
iv) Loans from related parties	KSh.'000	KSh.'000	KSh.'000	KSh.'000
Loan from related party (BATIF)	1,239,000	1,229,640	1,239,000	1,229,640

v) Key management compensation	2017	2016
	KSh.'000	KSh.'000
Salaries and other short-term employment benefits	135,526	136,065
Other long-term benefits	82,091	72,595
	217,617	208,660
vi) Directors' remuneration		
Fees for services as a director	18,101	17,385
Other emoluments (included in key management compensation above)	106,187	65,669
Total remuneration of Directors of the Company	124,288	83,054

NOTES (continued)

30. Contingent liabilities

The Group is a defendant in various legal actions. Based on professional advice received, the Directors are confident that the resolution of these cases is not likely to have a material effect on the financial statements.

The Group has guarantees amounting to KSh. 1,793,522,940 (2016: KSh. 1,711,709,740), issued on its behalf in the normal course of business from which it is anticipated that no material liabilities will arise.

31. Capital commitments

Capital expenditure contracted for at the statement of financial position date but not recognised in the financial statements is as follows:

	2017	2016
	KSh.'000	KSh.'000
Property, plant and equipment	171,670	79,250

PRINCIPAL SHAREHOLDERS AND **SHARE DISTRIBUTION**

Major Shareholders as at 15 February 2018

Shareholder	Total Shares	% Shareholding
Molensteegh Invest Bv.	60,000,000	60.00%
Standard Chartered Kenya Nominees Ltd,A/C Ke18993	13,631,824	13.63%
Standard Chartered Nominees Non-Resd. A/C 9866	2,970,023	2.97%
Standard Chartered Nominees Non-Resd. A/C Ke8723	1,340,900	1.34%
Kenya Commercial Bank Nominees Limited A/C 915A	965,223	0.97%
Kenya Commercial Bank Nominees Limited A/C 915B	730,045	0.73%
Standard Chartered Kenya Nominees Ltd A/C Ke23050	721,206	0.72%
Standard Chartered Nominees Resd A/C Ke11443	650,123	0.65%
Standard Chartered Nominees Resd A/C Ke11401	634,323	0.63%
Stanbic Nominees Ltd A/C Nr1030824	532,800	0.53%
Others (4,738 shareholders)	17,823,533	17.82%
TOTAL	100,000,000	100.00%

Summary of Shareholders as at 15 February 2018

Shareholder	No. of Shareholders	No. of Shares	% Shareholding
Foreign Companies	53	83,467,086	83.47
Foreign Individuals	85	211,290	0.21
Local Companies	476	10,641,880	10.64
Local Individuals	4,134	5,679,744	5.68
TOTAL	4,748	100,000,000	100.00

Distribution of Shareholders as at 15 February 2018

Shareholding	No. of Shareholders	No. of Shares	% Shareholding
Less than 500	2,501	556,084	0.56
501 - 5,000	1,842	2,921,103	2.92
5,001- 10,000	153	1,102,838	1.10
10,001 - 100,000	211	6,590,445	6.59
100,001 - 1,000,000	37	10,886,783	10.89
Above 1,000,000	4	77,942,747	77.94
TOTAL	4,748	100,000,000	100.00

Directors Shareholding as at 15 February 2018

Director	No. of Shares held
Sidney Wafula	300
Carol Musyoka	200


BRITISH AMERICAN
TOBACCO
KENYA

PROXY **FORM**

To: ....

The Secretary,
British American Tobacco Kenya plc,
P.O. Box 30000-00100,
Nairobi

I/We.. of P.O. Box .... member/members of British

American Tobacco Kenya plc appoint ....

or failing him, the Chairman of the Meeting as my/our proxy, to vote for me/us and on my/our behalf at the Annual General Meeting of the Company to be held on 11 May 2018 at 11:00am in the Ball Room, Hotel Intercontinental Nairobi, or at any adjournment thereof.

As witness my/our hand/s this .... day of.. 2018

....(Signature)

NOTES:

1. If a member is unable to attend this meeting personally this Form of Proxy should be completed and returned to The Co-operative Bank of Kenya Limited, Registrars Services, 1 Floor CIC Plaza II, Mara Road, Upper Hill, Nairobi or alternatively to the Registered Office of the Company so as to arrive not later than 2:30 p.m. on 9 May 2018. Duly signed proxy forms may also be emailed to shares@co-opbank.co.ke in PDF format.
2. A person appointed to act as a proxy need not be a member of the Company.
3. If the appointer is a corporation, this Form of Proxy must be under its Common Seal or under the hand of the officer or attorney duly authorised in that behalf.

BRITISH AMERICAN TOBACCO
KENYA

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