



Extending our **STRENGTHS**

Merchant Bank of Sri Lanka & Finance PLC | Annual Report 2017

MBSL successfully completed one of the significant and landmark mergers our nation has witnessed. This merger infused a sustainable competitive advantage giving us strength, scale, profitability and growth.

This unique position creates value advantages to our stakeholders; shareholders, investors, customers, employees and our community. With this advantage we soar into the future extending our advantage to maximize opportunities in the realm of financial services.

Vision, Mission and Values

Our Journey

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VISION

To be the most innovative business solution provider to the nation.

MISSION

To enhance our clients' wealth through innovative and sustainable solutions whilst developing entrepreneurship

To enhance shareholder value upholding highest standards of corporate governance

To enhance knowledge and skills of employees while rewarding them for achieving service excellence

To foster mutually beneficial relationships with our business partners

To fulfill our responsibilities towards the society by serving the nation while maintaining principles of corporate social responsibility

VALUES

Uphold the highest traditions of ethics, norms and best practices in all our endeavors

Guide our principles with wisdom and prudence in search of excellence

Foster intrapreneurship amongst our employees in creating an atmosphere of caring, sharing and integrity

Ensure good governance and transparency

Delight our clientele through service excellence, differentiation and innovation

Unite and be courageous to face challenges

OUR JOURNEY

1980

Operated as a management consultancy division of BOC.

1982

Formed as a limited liability company, the first Merchant Bank in Sri Lanka.

1989

Formed Lanka Securities [Pvt] Ltd, the first share brokering company in Sri Lanka.

1991

Listed in the Colombo Stock Exchange.

2016

"Best Employer Brand Award" in Sri Lanka Emerging Financial Institute of the year award.

2017

Asia's "Best Employer Brand" Award.

2017

International Europe Award for Quality.

2007

Annual Report Award.

2008

AA- Institutional Rating
"Silver Award – Joint" for Financial Institution.

2009

Took over MBSL Savings Bank and MBSL Insurance. Central Bank of Sri Lanka appointed MBSL as the managing agent of The Finance Company PLC.
"Bronze Award" for Financial Institutions.

2006

Obtained ISO 9001 – 2000 & National Productivity Award.

2005

Alliance with SBI Capital Markets Ltd – India.

2000

Obtained license from CBSL to operate as a leasing company Awarded Taiki Akimoto 5S [JASTECA].

1992

Took over Colombo Credit Ltd.

2017

The Company paved way for system change: Core Banking System.

2017

Award for the 100 Top Global HR Minds.

2017

Award for the “Best Service Provider” in HR.

2015

Amalgamation of MBSL , MCSL & MSB and started operations as a RFC.

“GOLD AWARD” for the annual report 2014 in the leasing sector.

Islamic finance and pawning operations expanded in some branches.

2012

30th Anniversary , opened up 16 new branches.

2014

Name Changed to “Merchant Bank of Sri Lanka & Finance PLC”.

“GOLD AWARD” for the annual report 2013 in the leasing sector.



About this Report

This is our 4th Integrated Annual Report and through it which aim to provide a concise yet comprehensive evaluation of how we created value to our multiple stakeholders. The Report has been prepared based on the principles of materiality, stakeholder inclusiveness, balance and conciseness as prescribed by the [Integrated Reporting] Framework published by the International Integrated Reporting Council (IIRC). The report covers the operations of Merchant Bank of Sri Lanka & Finance PLC (MBSL), its subsidiary namely MBSL Insurance Company Limited and associate Lanka Securities [Pvt] Ltd for the period from 1 January 2017 to 31 December 2017. We follow an annual reporting cycle and our most recent publication was for the period ending 31 December 2016. During the year there were no significant changes to the organization and or its supply chain.

Reporting Guidelines:

The Financial Statements have been prepared in accordance with Sri Lanka Accounting Standards and in conformity to of the Companies Act No.7 of 2007 and the Finance Leasing Act No.56 of 2000. For sustainability reporting, we have opted for the early adoption of the GRI standards in accordance "Core Criteria" published by the Global Reporting Initiative which will become effective in July 2018. The financial information presented herein reflects the consolidated numbers [unless otherwise stated] while the non-financial information relates to that of MBSL only.

Standards and External Assurance:

Assurance for the financial statements and Internal Controls has been provided by the Auditor General of Sri Lanka. External assurance for Sustainability Reporting has been provided by BDO Partners - Chartered Accountants.

Regulatory Compliance:

We also comply with regulations, directions and acts related to our various business activities. As a registered finance company, we conform to Finance Business Act No. 42 of 2011 and finance companies [Corporate Governance] directions. Product related legislations include Consumer Credit Act No. 29 of 1982, Finance Leasing Act No. 56 of 2000, the Right to Information Act No. 12 of 2016, Mortgage Act and Pawning Ordinance. The Corporate Governance and Risk Management reports comply with the stipulations applicable to the Registered Finance Leasing Establishments and Listing Requirements of the Colombo Stock Exchange. There were no restatements applicable for the information provided in the previous report.

Feedback:

We understand that Integrated Reporting is a journey of continuous improvement and welcome your suggestions. Please direct your feedback to,

Head of Finance

Merchant Bank of Sri Lanka & Finance PLC
BOC Merchant Tower,
No.28, St. Michael's road, Colombo-3
Tel: 0114711749
purnak@mbslbank.com



Navigating Our Report

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2017 in Numbers

Challenging macro-economic conditions and rising delinquencies in 2017 compelled the Company to revisit its strategy and refine its operating model to ensure the continued creation of value to its stakeholders. The year under review was therefore characterised by substantial changes, including the strengthening of credit appraisal, better digital capabilities and efforts to nurture a performance-driven culture. These timely management interventions have positioned the Company for strong and profitable growth over the medium to long-term and marks an important turning point in MBSL's history.

Financial Highlights

| | 2017 | Company 2016 | Change [%] |
|---------------------------------------|--------|-----------------|------------|
| Operating Performance [Rs. Mn] | | | |
| Net interest income | 2,448 | 2,028 | 21 |
| Gross income | 6,403 | 4,888 | 31 |
| Operating profit before tax | 464 | 578 | [20] |
| Profit before tax | 229 | 233 | [2] |
| Taxation | 128 | 154 | [17] |
| Profit after tax | 101 | 79 | 28 |
| Retained profit | 925 | 846 | 9 |
| Financial Position [Rs. Mn] | | | |
| Total assets | 35,645 | 31,927 | 12 |
| Gross loans and advances | 30,064 | 28,129 | 7 |
| Total deposits | 21,919 | 18,518 | 18 |
| Shareholders' funds | 3,234 | 3,107 | 4 |
| Operating Ratios [%] | | | |
| Return on average assets | 0.30 | 0.26 | 0.04 |
| Return on equity | 3.18 | 2.57 | 0.61 |
| Cost to income ratio | 73.10 | 71.89 | 1.21 |
| Non-performing loans ratio | 12.51 | 11.48 | 2.32 |
| Provision coverage | 33.24 | 30.92 | 2 |
| Loans to deposit ratio | 131.18 | 146.08 | [15] |
| Core capital ratio | 10.21 | 10.66 | [0.45] |
| Overall capital ratio | 15.27 | 10.69 | 4.58 |
| Shareholder Ratios | | | |
| Earnings per share [Rs.] | 0.61 | 0.47 | 30 |
| Net asset value per share [Rs.] | 19.50 | 18.73 | 4 |
| Price earnings ratio [Times] | 22.20 | 28.68 | [23] |
| Market price per share [%] | 13.50 | 13.60 | [1] |

Non-Financial Highlights

| | 2017 | 2016 | Change [%] |
|---|-----------|-----------|------------|
| Social and Relationship Capital | | | |
| No. of lending facilities | 82,620 | 77,742 | 6 |
| No. of deposits | 159,488 | 128,527 | 24 |
| Interest paid to customer (Rs. Mn) | 2,398 | 941 | 155 |
| Loans granted (Rs. Mn) | 17,862 | 18,369 | (3) |
| Customer touch points | 49 | 49 | - |
| New products launched | 4 | - | - |
| Investment in CSR (Rs. Mn) | 2.55 | 0.47 | 443 |
| Volunteer hours | 500 | - | - |
| Human Capital | | | |
| No. of employees | 968 | 917 | 6 |
| Payments to employees (Rs. Mn) | 1,015 | 788 | 29 |
| Investment in training (Rs. Mn) | 10 | 15 | (33) |
| Total training hours | 22,140 | 18,395 | 20 |
| Revenue per employee (Rs. Mn) | 6.61 | 5.33 | 24 |
| Retention rate [%] | 89 | 85 | 4 |
| National Development | | | |
| Contribution to the Government (Rs. Mn) | 272 | 178 | 53 |
| Loans outside the Western Province (Rs. Mn) | 17,726 | 15,961 | 11 |
| Micro finance disbursements (Rs. Mn) | 913 | 1,035 | (12) |
| Natural Capital | | | |
| Energy consumption (Units) | 1,369,892 | 1,269,818 | 8 |
| Energy consumption per employee | 1,468 | 1,385 | 6 |
| Water consumption (Units) | 15,350 | 17,616 | (13) |
| Paper usage | 394,924 | 315,960 | 25 |
| Paper recycled | 416 | 720 | (42) |
| Carbon footprint | 109,445 | 72,322 | 51 |

Chairman's Review



“The Company has placed strategic emphasis on strengthening its credit fundamentals including appraisal mechanisms, collections and recovery frameworks which are expected to support profitable growth in the long-term.”

Dear Shareholders,

It is my pleasure to set before you the Annual Report and Financial Statements of Merchant Bank of Sri Lanka & Finance PLC (MBSL) for the financial year ended 31 December 2017 and welcome you to the Annual General Meeting of the Company.

The Company performed commendably in a challenging year, achieving a revenue and profit growth of 31% and 28% respectively. Interest income growth was supported by the rising interest rate scenario during the year coupled with a credit portfolio expansion of 6%. The Company continued to capitalise on emerging opportunities in the country's small and medium enterprises sector through a customer-centric strategy. The subdued performance of the country's agriculture sector together with the moderating macro-economic conditions resulted in a weakening of credit quality and we have taken proactive efforts to address these emerging pressures. The Company has placed strategic emphasis on strengthening its credit fundamentals including appraisal mechanisms, collections and recovery frameworks which are expected to support profitable growth in the long-term.

It is important to set our performance in the context of the operating environment that prevailed during the year; Sri Lanka's economic growth slowed to 3.1% in 2017, reflecting a relatively tight fiscal and monetary policy stance and a subdued agriculture sector which continued to be affected by adverse weather. The CBSL raised the Standard Deposit facility rate to 7.25% in September 2017 compared to 7% in 2016 and the standard lending rate increased to 8.75% in September 2017 compared to 8.5% in 2016. This resulted in a gradual increase in market interest rates for latter part of the year. Despite the

tighter monetary policy stance, inflation rise gradually during the year reflecting VAT revisions in 2016, rising international commodity prices and supply constraints of agricultural produce. Despite these short-term pressures, we remain optimistic on the growth potential presented by the stabilising macro-economic conditions as policy reforms, strengthening government finances and improving international relations lay a firm foundation for long-term economic development.

The Company's Board of Directors combine diverse skills and industry acumen, representing entrepreneurial, professional and academic experience. Key regulatory developments during the year included the implementation of a new framework on guidelines for client protection and revisions to the Loan to value ratio on leasing. The Company was fully compliant with all relevant regulations and guidelines during the year and continues to demonstrate the highest standards of integrity, corporate conduct and ethics.

During the year, we welcomed Mr. Nishaman Karunapala as the new Chief Executive Officer. Our team of 968 employee is key to our success and we continued to invest in enhancing our employee value proposition through providing opportunities for career and skill development. Efforts were made to nurture a performance-driven culture through strengthening the KPI framework across the organisation. These efforts have been rewarded with a relatively high retention rate of 89% and the Company once again being awarded the Asia's Best Employer Brand in 2017.

The Board is of the view that Sri Lanka's insurance industry presents significant upside potential given the relatively low penetration levels. We have therefore decided to retain a controlling interest in our insurance arm, MBSL Insurance

which has obtained both life and general insurance licenses. The Company intends to revive MBSL Insurance in partnership with a significant minority equity partner. Expressions of Interest (EOI) have already been called with several positive responses. A collective capital infusion to the tune of Rs.1.2 billion is expected over the short to medium term.

I look forward to another exciting year of opportunities and progress and would like to extend my gratitude to the Minister, Secretary and officials of the Ministry of Public Enterprises, the officials of the Treasury and non-bank supervision department of the Central Bank of Sri Lanka and the Board of Directors of Bank of Ceylon. I thank my colleagues on the Board of MBSL and extend my gratitude to Mr. C.N Wijewardane and Mr. H.J.D Fonseka who resigned from the Board during the year. Finally, my gratitude goes out to the management and all employees of MBSL for their commitment and dedication and all our customers and other stakeholders for their continued support.

Thank you.



Dr. Sujeewa Lokuheewa
Chairman

17 May 2018
Colombo

About Us

Overview

MBSL entered the Sri Lankan financial sector as the country's pioneer merchant bank in 1982. Subsequently re-registered as a licensed finance company under the Companies Act of 2007, MBSL now functions under the regulatory purview of the Central Bank of Sri Lanka. The Company's key business activities include Leasing, Loans, Corporate Advisory & Capital Markets, Trade and Project Finance, Pawning, Real Estate and Deposit Mobilisation. We engage with customers through a widespread network of 49 customer touch points in 22 districts. The Company caters to a segment that is generally overlooked by the formal banking system and have transformed the lives of thousands of people by providing accessing to finance and facilitating socio-economic empowerment. The Company's fully-owned subsidiary MBSL Insurance is engaged in the provision of general and life insurance solutions. MBSL is a subsidiary of the state-owned financial powerhouse Bank of Ceylon, Sri Lanka's largest licensed commercial bank in terms of assets, deposits and branch reach.

Assets

Rs. **35,645** Mn
[2016 Rs. 31,927 Mn]

Deposits

Rs. **21,919** Mn
[2016 Rs. 18,518 Mn]

Employees

968
[2016 - 917]

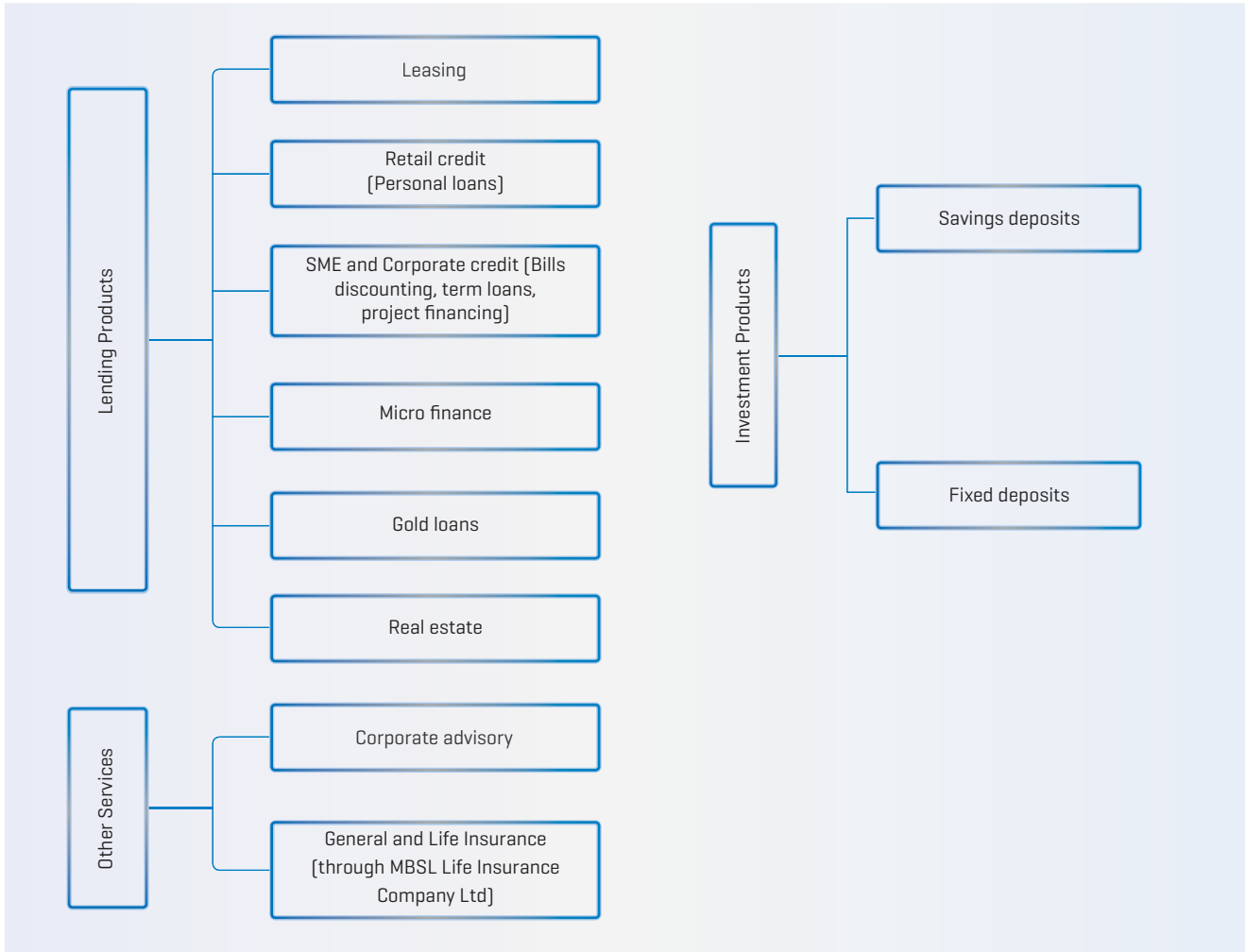
Customer touch points

49

Market capitalisation

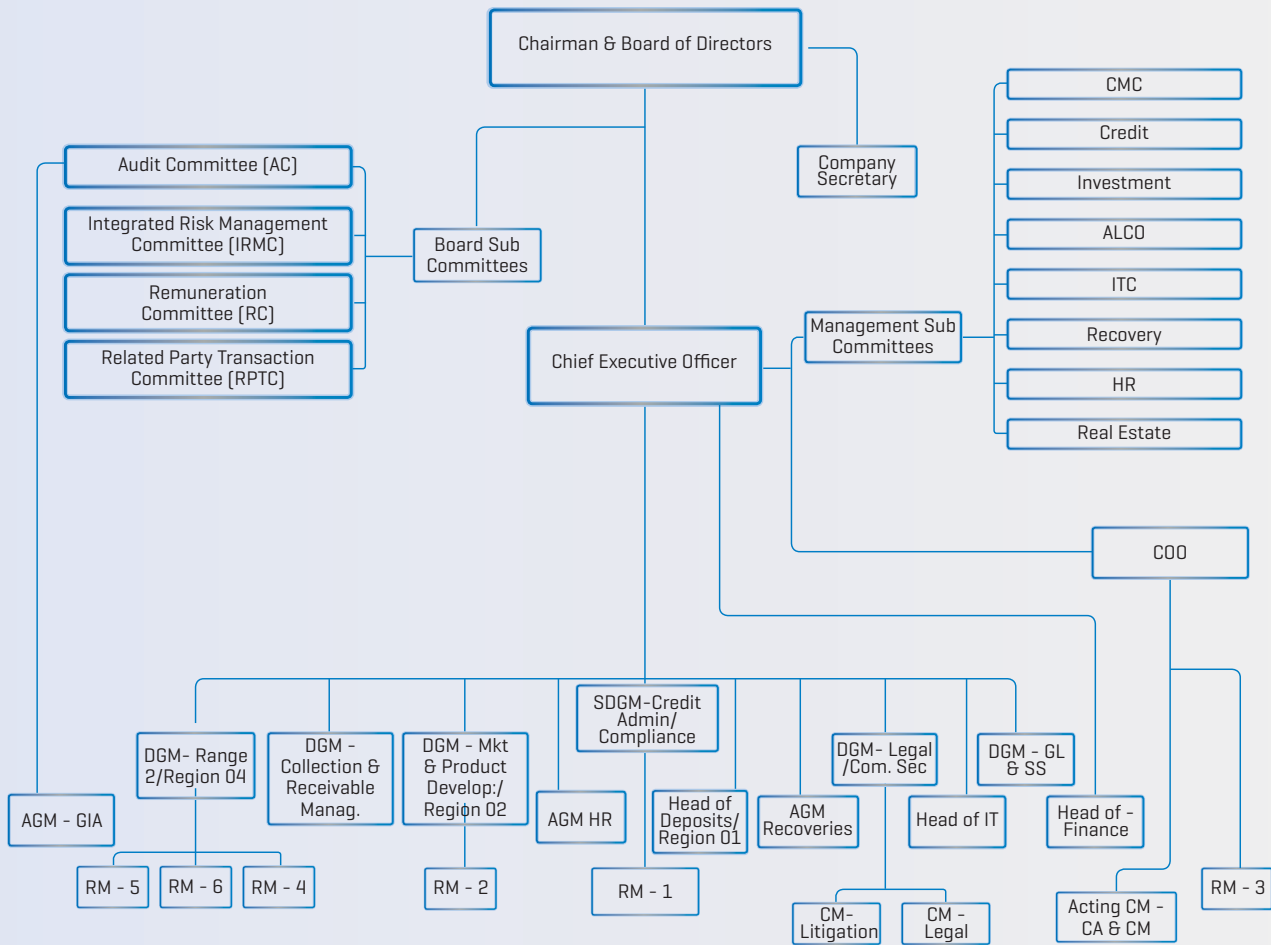
Rs. **2.24** Bn

Our Products and Services



Organization Structure

Corporate Management & Regional Structure-Merchant Bank Of Sri Lanka & Finance PLC



Awards and Recognition



- Asia's Best Employer Brand Award 2017 - World Human Resource Development Congress – Singapore.
- International Europe Award for Quality 2017 - Global Trade Leaders' Club – France.
- Emerging Financial Institute of the year 2017 - Middle East Asia Leadership Summit.
- Best Service Provider in HR 2018 - Global HR Excellence Awards – India.
- 100 Top Global HR Minds 2018 - Global HR Excellence Awards – India.



Charting Our Progress

Value Creation Model

RESOURCES WE UTILISED

Financial Capital

Represents our source of asset funding.
 Rs. 3.2 Bn Equity capital
 Rs. 31.3 Bn Debt capital
 [Page 29]



Manufactured Capital

Support customer engagement, service delivery and enhance convenience of banking.
 [Page 36]



Human Capital

Pool of 968 employees
 [Page 38]



Intellectual Capital

Consists non-monetized assets such as brand image, trust, confidence and relationships.
 [Page 43]



Social and Relationship Capital

Customers drive our business model.
 [Page 45]



Natural Capital

Sustainability continues to be an important part of our responsible growth.
 [Page 49]



VALUE CREATING PROCESSES

Value Creating Processes

Our Products

Deposit Mobilisation

Lending Activities

Capital Markets and Corporate Advisory

General and Life Insurance Solutions

Strategic Priorities

Growth and Profitability

Customer Centric

Empowered Workforce

01

02

03

VALUE CREATING PROCESSES

Service Delivery



49

Customer Touch Points



968

Employees

Customer Base

19,245

Leasing Customers

22,601

Micro Entrepreneurs

148,549

Depositors

4,428

Term Loan Customers

20,903

Personal Loan Customers

5,103

Pawning Customers

Strategic Priorities

Governance and Risk Management

Sustainability

04

05

OUTPUTS AND OUTCOMES

Shareholder
Value Creation



Profit Attributable

Rs. **100.8** Mn

Earnings Per Share

Rs. **0.61**

Employee
Value Creation



Payments to Employees

Rs. **1,015** Mn

Training Hours

22,140

Customer
Value Creation



Loans Disbursed

Rs. **17,862** Mn

Interest Paid

Rs. **2,398** Mn

Government



Tax Contributions

Rs. **272** Mn

Micro Finance Disbursement

Rs. **913** Mn

Community



Investment in CSR

Rs. **2.55** Mn

Environmental
Impacts



Paper Recycled

416 Kg

Carbon Footprint

109,445 Kg

Stakeholder Engagement

Connectivity with stakeholders is important for performance and development of the organization. In selecting stakeholder groups to engage with, we focus on entities and individuals who are significantly affected by our operations. Key stakeholder groups identified are shareholders, employees and customers while relationships with other external stakeholders such as government, local communities and other financial institutions play an essential role in the continuity of our operations.

The Company's key engagement mechanisms and areas of discussion during the year are given below;



Shareholders

The largest shareholder is BOC accounting for a share of 74.49% in the Company. The remainder is held by institutional and retail investors.

| Modes of Engagement | Key Topics | Our Response in 2017 |
|--|---|---|
| <ul style="list-style-type: none"> Annual general meeting Annual report Quarterly financial reports Media releases and press conferences | <ul style="list-style-type: none"> Financial performance Sustainable growth Adequate returns Sound governance and risk management practices Business expansion Portfolio diversification Compliance with new regulations | <p>The strategic initiatives in 2017 focused on improving the credit quality of the loan portfolio by developing KPIs that focused on sales centricity and credit recovery</p> <p>1 2 3 4</p> |



Customers

Our diverse customer base comprises more than 72,000 individuals, micro enterprises, SMEs and corporates.

| Modes of Engagement | Key Topics | How We Addressed |
|--|---|--|
| <ul style="list-style-type: none"> Face to face interactions at branches Routine marketing campaigns Ongoing customer workshops Annual reports Social media Press releases | <ul style="list-style-type: none"> Security of deposits Competitive interest rates Customer service Convenience of banking Digitisation Financial inclusion Responsible lending and business practices | <p>Made efforts to nurture a customer centric and sales driven culture within the organization with sales-oriented targets and routine marketing campaigns through branches to target new customers and deepening relationships with existing clientele</p> <p>2</p> |



Employees

Our talent pool comprises 968 employees.



Government and Regulatory Authorities

MBSL falls under the regulatory purview of the Central Bank of Sri Lanka, Securities and Exchange Commission, Department of Inland Revenue, Colombo Stock Exchange and Ministry of Public Enterprises Development.



Suppliers



Communities

The communities in which we operate

| Modes of Engagement | Key Topics | Our Response |
|---|---|---|
| <ul style="list-style-type: none"> • Annual performance appraisals • Monthly staff meetings • Meetings with trade unions on a need basis • Social and welfare events • Intranet • Corporate website • Written communication such as circulars and directions | <ul style="list-style-type: none"> ➤ Key performance indicators ➤ Remuneration package ➤ Employment practices ➤ Training and development ➤ Compliance with employment laws and regulations | <p>During the year we focused on empowering our workforce by implementing a performance driving culture with KPIs being of set for all staff members</p> <p>3</p> |
| <ul style="list-style-type: none"> • Written communications such as directions and circulars • Press releases [ongoing] • Meetings [when required] | <ul style="list-style-type: none"> ➤ Contributions towards policy discussions and forums affecting the industry ➤ Responsible business practice ➤ Compliance to rules and regulations | <p>We maintain a continuous and open dialog with our regulators, engaging with all relevant authorities in contributing to the development of the industry</p> <p>4</p> |
| <ul style="list-style-type: none"> • Supplier registration [ongoing] • Supplier relationship management [ongoing] • Onsite visits and meetings [ongoing] | <ul style="list-style-type: none"> ➤ Ease of transactions ➤ Value addition and supplier development ➤ Long-term partnerships ➤ Quality of service | <p>We strive to establish long-term, mutually beneficial relationships with our suppliers</p> <p>5</p> |
| <ul style="list-style-type: none"> • CSR initiatives [when requested] • Sponsorships [ongoing] • Press releases [ongoing] | <ul style="list-style-type: none"> ➤ Employment generation ➤ Provision of financial solutions ➤ Responsible business practices ➤ Community development | <p>Our community engagement initiatives are directed towards empowering and uplifting the living standards of the people in the communities we operate in</p> <p>5</p> |

Risks and Opportunities

The Group's strategy is formulated following an assessment of emerging risks and opportunities in the operating landscape. We ensure that our strategy positions us to capitalise on the opportunities while strengthening governance and risk management structures to minimise the impacts of emerging risks.

Macro-Economic Conditions

Sri Lanka's economic growth moderated in 2017, with GDP growing by 3.1% during the year. The Agriculture sector continued to disappoint, affected by adverse weather conditions while the Industry and Services sectors expanded by 3.9% and 3.2% respectively. The weakening of the Agriculture sector has in turn affected the Financial sector, with the repayment ability being pressured. [Refer to page 22 for further information]

Regulatory Developments

Persistently increasing regulatory and compliance requirements have led to increased complexity and higher compliance costs. During the year, a 'Financial Customer Protection Framework' was introduced for all LFCs and SLCs to ensure the protection of rights and interests of financial customers. The framework includes specific guidelines on Disclosure and Transparency, Customer Education & Awareness, Responsible business conduct, Complaint handling and Customer privacy among others. A new capital adequacy framework encompassing a more risk sensitive focus on covering credit and operational risk is also expected over the medium term. This is expected to encourage a natural consolidation drive, pushing weaker institutions to merge with larger players

Emphasis on Sustainability Considerations

Increasingly serious implications of climate change are demonstrating how human consumption patterns can affect the planet's sustainability. Erratic weather patterns, rising temperatures and energy constraints impacting economic growth in several regions. On the other hand, millions of citizens around the world still lack access to employment opportunities, affordable housing, transportation, education and healthcare. Financial institutions have an important role to play in addressing these issues and driving economic, social and environmental progress. In addition to minimising their own environmental impacts, financial institutions play a vital role in supporting environmentally and socially responsible initiatives through their lending practices; these include lending towards renewable energy, green technology, women's empowerment and rural development among others

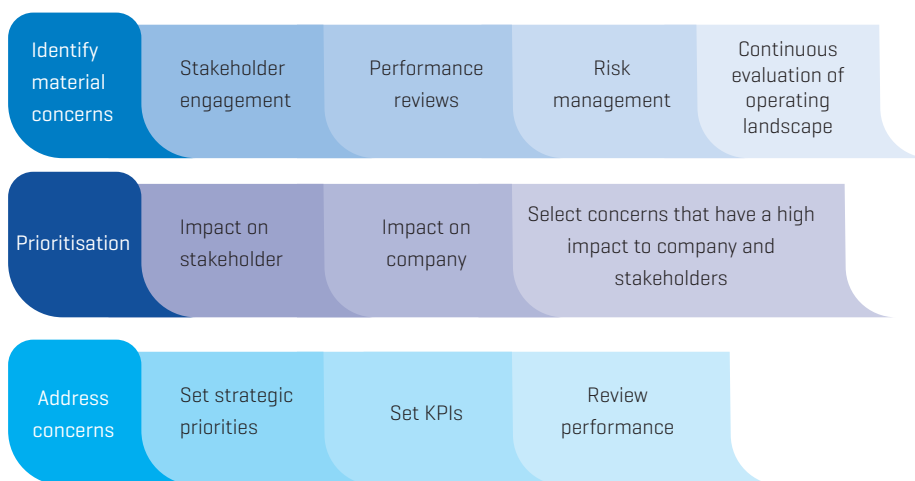
Increasing Connectivity

Sri Lanka's internet subscribers have more than tripled over the past 3 years and mobile penetration is more than 100%, demonstrating the level of digital literacy in the country. This connectivity has presented numerous opportunities for the financial sector and transformed the way institutions interact with their customers. Digital capabilities will therefore be crucial driving differentiated value

Determining Material Topics

The content to be included in this report was determined following a systematic process of materiality analysis to ensure that we discuss the factors that have the most significance to our stakeholders. These issues are defined as material issues and consist of aspects that could potentially have the most significant impact on the Group’s ability to create value and stakeholder concerns identified through the Stakeholder Engagement process described on page 16 of this report. Material issues play a vital role in determining our strategy and business activities. There has been no significant changes to material topics compare to the previous year.

The Group’s material topics for the year under review are given in the matrix below; the topics highlighted in blue represent material concerns and are reported fully in this report.



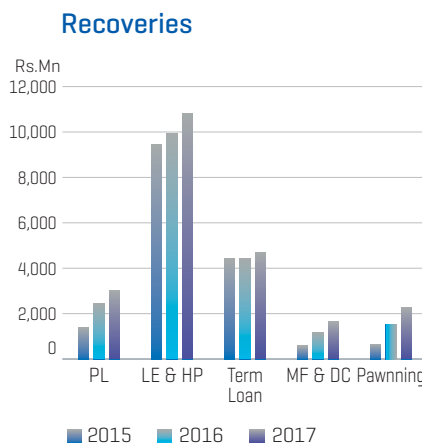
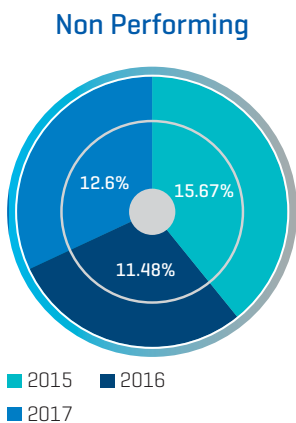
| Strategic priorities | MATERIAL CONCERNS IN 2017 | | | | | |
|--------------------------------|--------------------------------------|---|------------------------------------|---------------------------------|---------------------|--------------------------------|
| | GRI indicators covered in the report | | | | | |
| Profitability | Financial Performance | Market Reach | Process efficiency | NPL management | Government policies | Diversification |
| Customer centric | Service delivery | Trust and confidence | Customer privacy | Competitive offerings | Digitisation | Responsible lending |
| Employee empowerment | Training and development | Industrial relations | Culture and attitudes of employees | Diversity and equal opportunity | Employee engagement | Occupational health and safety |
| Governance and risk management | Compliance | Risk management | Governance practices | Credit quality | Changing regulation | |
| Sustainability | Responsible lending | Regulatory requirements such as customer relationship framework | Community engagement | Effluents and waste | Climate action | Minimize environmental impact |

Strategic Framework

Pursuing customer growth and credit recoveries from existing clientele was challenging in 2017 as competition intensified and macro policies were unconducive to credit growth and pressurized the affordability of customers. The strategy for the year 2017 was focused on realigning our processes to support business growth and our sustainability objectives despite the challenging operating landscape. A performance driven culture was the underlying driver of our strategy that connected performance to organizational goals through measurable KPIs. Continuous performance evaluation and increasing awareness of KPIs ensured that the efforts and performance of all employees contributed towards our medium-term goals.

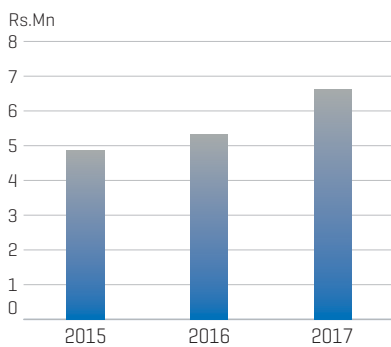


| Growth and Profitability | | Cost management initiatives to improve profitability | | |
|--------------------------|--|---|---|--|
| Initiatives | Strengthen credit underwriting | Increase recoveries | Sustainable growth | |
| | Revised customer screening criteria | Streamlined recovery processes with dedicated resources deployed for specific categories of outstanding receivables | Pursued growth in the advances through increasing penetration in pawning as well as two and three wheeler financing | |
| | Nurtured a more responsible culture of lending through employee training and awareness | Introduced KPI and collection targets for credit recovery | | |
| KPI | Strengthened credit risk management | Total recoveries during the period | Portfolio growth | |
| | Non-performing loans as % of total loan portfolio | | | |

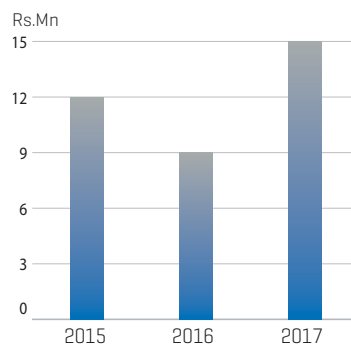


| | | | |
|----------------------------|---|--|---|
| Customer Centricity | Nurturing better customer relationships through extending the reach and enhancing service excellence. | | |
| Initiatives | Sales driven workforce | Increase marketing campaigns | Digitisation |
| | Employees were trained to adopt to a market driven approach with sales oriented KPIs | Routine marketing campaigns were conducted by branches | The successful implementation of the core banking platforms has positioned the group to capture opportunities in digital propositions |
| KPI | Revenue per employee | Investment in branding | New customers by product and sector |

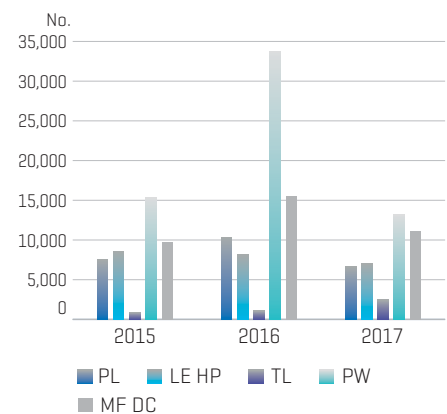
Revenue per Employee



Investment in Branding



New Facilities

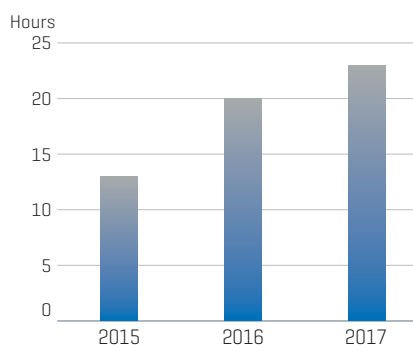


Employee Empowerment

Drive a performance driven culture within the organization

| | | | |
|-------------|---|--|---|
| Initiatives | Training and development | Engagement | Performance management |
| | Intense focus on training and development internal and external | Maintained cordial relationships with trade unions during the year | Continuous monitoring of KPIs and shared information provided in the management Information system with employees |
| KPI | Training hours per employee | No grievance and trade union action during the year | |

Training Hours per Employee

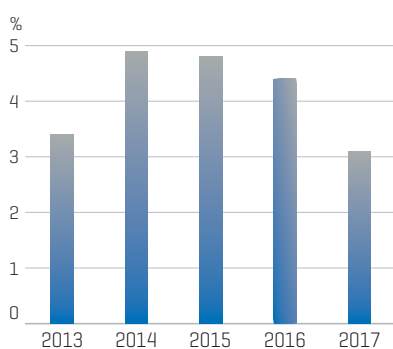


Economic and Industry Environment

| Macro-economic variable | Impact on MBSL |
|-------------------------------------|---|
| Weakening of the agriculture sector | Affected the repayment ability of our agriculture sector borrowers, leading to increased delinquencies |
| Increasing interest rate scenario | Pressure on NIMs given the inherent asset liability maturity mismatch and the faster repricing of deposit liabilities |
| Higher inflation | Adversely impacted consumer spending leading to difficulties in collection |

Sri Lanka's economic growth slowed to 3.1% in 2017, reflecting a relatively tight fiscal and monetary policy stance and a subdued agriculture sector which continued to be affected by adverse weather. The agriculture sector contracted by 0.8% and had cascading effects on other sectors of the economy. The Industrial sector recorded moderate growth, expanding by 3.9% supported by the relatively strong performance in manufacturing activities. The Service sector, which has the highest contribution to the country's GDP grew by 3.1% during the year, with the financial services sub-sector expanding by 9.4%.

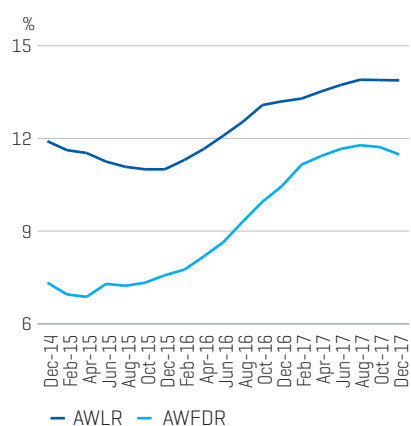
GDP Growth



Interest rates: The Government adopted a relatively tight monetary policy stance in 2017, with the objective of controlling inflationary pressures. The Standard Deposit facility rate was increased to 7.25% in September 2017 compared to 7% in 2016 and the standard lending rate increased to 8.75% in September 2017 compared to 8.5% in 2016. This resulted in a gradual increase in market interest rates

for latter part of the year. The Government also pursued fiscal consolidation, resulting in an increase in tax rates which led to a slowdown in private consumption expenditure.

Interest Rates



Inflation: Despite the tighter monetary policy stance, inflation rose gradually during the year reflecting VAT revisions in 2016, rising international commodity prices and supply constraints of agricultural produce. Accordingly, the Headline National Consumers' Price Index (NCPI) fluctuated between 6.5% and 7.3% [y-o-y] during the year. The CBSL's plans to move towards a flexible inflation targeting regime over the medium term is anticipated to support macro-economic stability, facilitating sustained low inflation underpinned by improvements in monetary and fiscal policy.

Outlook: Political instability following the recently concluded local council elections and government attempts to

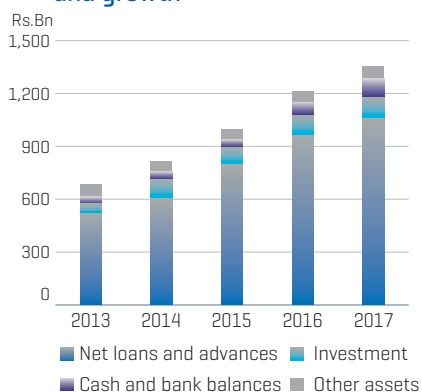
achieve fiscal consolidation is expected to affect the country's short-term growth prospects. Over the longer-term however, policy reforms, stabilisation of government finances and improving international relations are expected to lay a firm foundation for long-term economic development.

The Non-Bank-Financial Institutions Sector

Sri Lanka's NBF sector comprises forty-five Licensed Finance Companies (LFCs) and six Specialized Leasing Companies (SLCs). The sector plays a critical role in facilitating access to finance and encouraging entrepreneurship in a relatively risky customer segment which is often overlooked by the banking sector.

Asset growth: The Sector's total asset growth moderated to 12% [y-o-y] as the core lending portfolio of leasing was affected loan-to-value restrictions and the rising interest rate scenario which prevailed for most part of the year. Total gross loans and advances thus increased by 10% in 2017, with the growth rates of the leasing and loan portfolios decelerating during the year under review. Resultantly LFCs shifted focus to other lending categories such as pawning advances, which increased by 29% in 2017.

Sector asset composition and growth



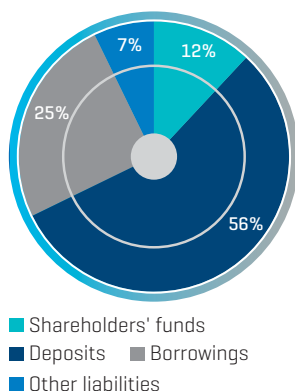
SOURCE: CBSL

Portfolio quality: Lending institutions witnessed a deterioration in credit quality, with NPLs increasing by 24% (y-o-y) during the year due to unfavourable weather conditions and rising inflation affecting the performance of several economic sectors. Agriculture sector customers also faced repayment pressure, resulting in higher delinquencies from the segment. Resultantly, the sector’s gross NPA increased to Rs. 65.9 Bn in December 2017, compared to 24% the year before. Loan loss provisions increased by 18% during the year with the provisioning coverage ratio maintained 64% marginally below last year.

Funding and liquidity: The Sector’s total deposit base increased by 29% during the year and accounted for 51% of the total liabilities as at end-December 2017. Borrowings declined by 10% (y-o-y) and accounted for 29% of the sector’s liabilities. The total capital base widened by 16% and contributed 14% to the total funding composition. The Tier 1 capital base formed 95% of the regulatory capital base, benefitting from the growth in retained profits as financial institutions undertook initiatives to progressively comply with Basel III Minimum Capital Requirements. The Core Capital adequacy ratios improved marginally to 12.4% during the year while

the total capital adequacy ratio amounted to 13.1% by end-December 2017, remaining comfortably above regulatory thresholds.

Funding Composition



Profitability: The sector’s total interest income increased by 23% (y-o-y) supported by credit growth and the rising interest rate scenario. However, net interest margins were impacted by higher cost of funding as rising market interest rates, which led to interest expenses increasing by 32% (y-o-y). Total non-interest expenses costs increased by 22% (y-o-y) in 2017 further pressurising profitability. Profitability weakened due to increasing costs and profit after tax declined by 18% (y-o-y) to Rs.25.8 billion. Return on Equity (ROE) declined to 16.1% compared to 23% the previous year.

Liquidity: The relatively slow loan growth during the year resulted in deposit liabilities being channelled towards liquid assets.

Regulatory framework

In 2017, a ‘Financial Customer Protection Framework’ was introduced for all LFCs and SLCs to ensure the protection of rights and interests of financial customers. The framework includes specific guidelines on Disclosure and Transparency, Customer Education & Awareness, Responsible business conduct, Complaint handling

and Customer privacy among others. A new capital adequacy framework is also expected to be implemented encompassing a more risk sensitive focus on covering credit and operational risk under the basic approach of the BASEL accord. This is expected to encourage a natural consolidation drive, pushing weaker institutions to merge with larger players. Further regulations are also expected on corporate governance, risk management, liquidity and provision regulations. Additionally, financial institutions are required to adopt to Sri Lanka Financial Reporting Standard – 9, Financial Instruments (SLFRS 9) in January 2018, requiring a change in the recognition of loan loss provisions.

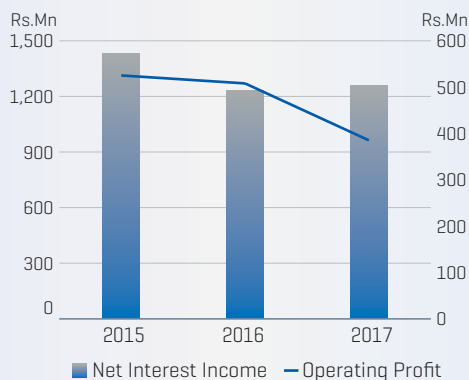
Our Performance

Operational Reviews

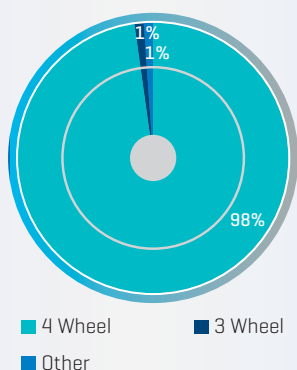
Performance Highlights 2017

| | 2017 | 2016 | % |
|------------------------------|--------|--------|------|
| Revenue (Rs. Mn) | 3,044 | 2,511 | 21 |
| Net interest income (Rs. Mn) | 1,433 | 1,231 | 16 |
| Impairment charge (Rs. Mn) | 114 | 24 | 380 |
| Operating profit (Rs. Mn) | 522 | 508 | 3 |
| Assets (Rs. Mn) | 15,661 | 14,992 | 4 |
| Liabilities (Rs. Mn) | 13,750 | 12,843 | 7 |
| Gross NPL ratio (%) | 8.19 | 7.07 | 1.12 |
| Cost to income ratio (%) | 62 | 58 | 4 |
| Portfolio outside the WP (%) | 69 | 67 | 2 |

Leasing



Portfolio Composition



Leasing

Operating Environment in 2017

Restrictions on the LTV ratios, depreciation of the exchange rate and the gradual uptick in interest rates affected demand for leasing facilities during the year. Moderating economic conditions and the subdued performance of the agriculture sector also impinged on portfolio quality, with a general weakening of credit quality across the industry.

Strategic Initiatives

- Emphasis on strengthening and streamlining collection mechanisms including the introduction of collection KPIs
- Enhanced recovery framework with dedicated teams handling outstanding classified by aging
- Entered the two and three-wheeler leasing segment
- Intense employee training on credit risk consciousness, credit appraisal and collections among others

Performance

Growth of the Company leasing portfolio slowed to 4% in 2017, reflecting challenging market conditions as well as the Company efforts to consolidate its existing portfolio. Resultantly, interest income from leasing increased by only 21% during the year and accounted for 49% of total interest income. We achieved increased diversity in our leasing book, following the entry into the two and three-wheeler segment.

A combination of factors including the moderating economic conditions, relatively lax credit practices in previous periods and weakening of the country's agriculture sector adversely impacted MBSL's portfolio quality; the leasing segment experienced a 18.07% increase in non-performing-loans, translating to a gross NPL ratio of 8.19% as at end-December 2017. However, proactive efforts to stem a further increase in NPLs and efforts to improve the fundamental credit quality have already begun to bear fruit with significant improvements seen in collections towards the last months of the year.

Resulting from the above developments, the leasing division's profit for the period increased by 3.6% to Rs. 18.28 million; despite the decline leasing continues to be the largest contributor to Company profitability.

Outlook

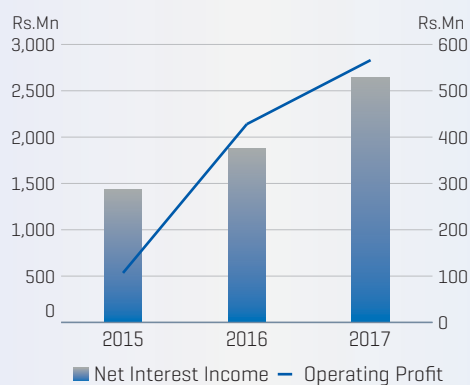
Over the short-to-medium term, we will place strategic focus on increasing lending to hybrid and electric vehicles in a bid to achieve our business and sustainability objectives. Our growth plans are ambitious, but parallel focus will be placed on preserving underlying credit quality through the initiatives launched in the reviewed period. This is further facilitated by the access to real-time, holistic information enabled by the core banking platform.

Operational Reviews

Performance Highlights 2017

| | 2017 | 2016 | % |
|------------------------------|--------|--------|----|
| Revenue (Rs. Mn) | 2,648 | 1,876 | 41 |
| Net interest income (Rs. Mn) | 1,319 | 955 | 38 |
| Impairment charge (Rs. Mn) | 186 | 0.40 | - |
| Operating profit (Rs. Mn) | 566 | 428 | 32 |
| Assets (Rs. Mn) | 13,130 | 12,156 | 8 |
| Liabilities (Rs. Mn) | 11,527 | 10,414 | 11 |
| Gross NPL ratio [%] | 17.69 | 16.74 | 1 |
| Cost to income ratio [%] | 56 | 55 | 1 |
| Portfolio outside the WP [%] | 47 | 40 | 7 |

Interest Income & Operating Profit



Corporate and Retail Credit

Operating Environment in 2017

Credit growth slowed due to the moderating economic conditions and rising interest rates particularly during the latter part of the year. Meanwhile, increasing funding costs affected NIMs across the industry while portfolio quality also weakened, thereby impacting overall profitability.

Strategic Initiatives

- Curtailed exposure to unsecured lending and loan categories giving rise to high delinquencies
- Pursued aggressive growth in pawning
- Emphasis on strengthening and streamlining collection mechanisms including the introduction of collection KPIs
- Sought customer acquisition through more frequent sales campaigns carried out by branches
- Revised credit policy to define target markets clearly; for instance, in the salaried employees segment, we will focus primarily on the government sector and relatively established organisations, as opposed to a relatively risky segment

Performance

The corporate and retail credit portfolio expanded by 9% during the year supported by commendable growth in personal loans (14%) and pawning (40%) while growth in the microfinance and term loans segments were curtailed. Resultantly, the segment's interest income expanded by 41% during the year.

Expanding the pawning portfolio is a key short to medium term priority and during the year we laid the foundation to pursue this growth. We strengthened our pawning team, conducted comprehensive training programmes, improved the performance management system and enhanced the operational risk management framework to strengthen internal controls. We hope to further strengthen the customer proposition through expanding our geographical reach and increasing accessibility through providing extended service hours.

Portfolio quality weakened during the year, with increased delinquencies stemming from unsecured loans and micro-financing facilities. Resultantly, exposure to these products were curtailed, with certain products being completely discontinued in a bid to stem the rising NPLs. The segment's gross NPL ratio increased to 17.69% from 16.74% the year before. That said, organisation-wide efforts to strengthen underlying portfolio quality is expected to bear fruit over the medium term, facilitating a sustained improvement in portfolio quality.

Outlook

The pawning segment presents ample opportunities for growth, and we hope to pursue strong expansion in this lucrative segment. We will adopt a cautious approach when engaging in unsecured lending and have revised our credit policies to reflect this stance. Preserving portfolio quality is an organisation-wide effort and we will continue to up skill employees in nurturing a credit conscious culture.

Corporate Advisory

Performance Highlights 2017

| | 2017 Rs.Mn | 2016 Rs.Mn | % |
|---------------------|---------------|---------------|------|
| Revenue | 21 | 18.47 | 11 |
| Net interest income | (12) | (31) | 62 |
| Other income | (11) | (22) | 52 |
| Operating profit | (34) | (142) | 76 |
| Assets | 238 | 373 | (36) |

Operating Environment in 2017

Sri Lanka's stock market performance reversed its declining trend to record marginal improvement during the year. The All Share Price Index increased by 2.3% in 2017, compared to a 9.7% decline in 2016. The S&P Index also increased by 1.3% during the year.

Strategic Initiatives

- Independent opinion on Multi Finance PLC
- Rs.2.0 billion debenture issue for MBSL
- Seminar on the introduction to Blue Ocean strategies

Performance

The division offers a broad range of advisory and capital market related services which include portfolio management, provision of capital market related services (such as structuring and management of equity, debt issues and private placements) and Corporate Advisory services. The unfavourable equity market conditions over the last few years had compelled the division to curtail its activities and reduce exposure to the stock market. During the year the division reduced its' operating losses to Rs.33.73 million compared to Rs. 142.34 million the year before.

We see significant growth potential in this segment over the medium to long-term, given the country's improving macro-economic fundamentals and anticipated

inflow of foreign investments. In 2018 we hope to deploy additional resources to this division and sharpen our strategic focus to capitalise on these growth opportunities.

Economic Value Addition

The Company is committed to transforming its capital inputs in a way that generates sustainable value for all our stakeholders. The economic value created by the Company is shared between its shareholders, employees, tax contributions to the government and other stakeholders while a portion of it is retained for the Company's future growth. This is reflected in the Economic Value Added statement below.

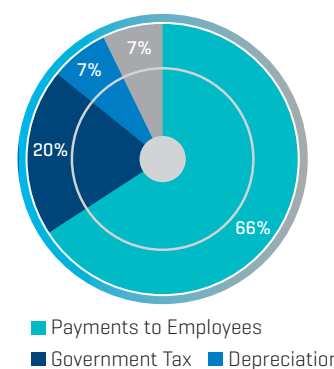
Statement of Value Added

| Company | 2017 Rs. Mn | 2016 Rs. Mn |
|---------------------------------------|----------------|----------------|
| Value Added | | |
| Gross Value added | 6,403 | 4,888 |
| Cost of borrowings & support services | (4,559) | (3,429) |
| Provision for bad debts & investments | (300) | (257) |
| | 1,544 | 1,202 |
| Value Allocated | | |
| Payments to Employees | 1,027 | 782 |
| Government tax | 307 | 266 |
| Depreciation | 109 | 75 |
| Retained Earnings | 101 | 79 |
| | 1,544 | 1,202 |

Sources & Utilization of Income

| | 2017 Rs. Mn | 2016 Rs. Mn |
|---|----------------|----------------|
| Sources of Income | | |
| Interest income | 6,157 | 4,738 |
| Fee & Commission income | 180 | 131 |
| Dividend income | 8 | 13 |
| Other income | 58 | 6 |
| | 6,403 | 4,888 |
| Utilization of Income | | |
| Payment to lenders | 3,709 | 2,710 |
| Payments to employees | 1,027 | 782 |
| Support services | 850 | 720 |
| Retained earnings | 101 | 79 |
| Depreciation & Amortization | 109 | 75 |
| Impairment charges for loans and other losses | 300 | 257 |
| Government taxes | 307 | 266 |
| | 6,403 | 4,888 |

Value Allocation





Customer-centric strategies

Financial Capital



2017 was a year of mixed fortunes for the Company, characterised by relatively strong portfolio and revenue growth which was countered by increasing impairment charges. During the year significant focus was placed on strengthening the credit fundamentals and restructuring our processes to ensure profitable growth over the medium to long-term.

Highlights of 2017

| | 2017 | 2016 | y-o-y % |
|------------------------------|--------|--------|---------|
| Interest income [Rs. Mn] | 6,157 | 4,738 | 30 |
| Net interest income [Rs. Mn] | 2,448 | 2,028 | 21 |
| Impairment [Rs. Mn] | 244 | 24 | 908 |
| Pre-tax profit [Rs. Mn] | 229 | 233 | (2) |
| Post tax profit [Rs. Mn] | 101 | 79 | 28 |
| Total assets [Rs. Mn] | 35,645 | 31,927 | 12 |
| Deposits [Rs. Mn] | 21,919 | 18,518 | 18 |
| Shareholders' funds [Rs. Mn] | 3,234 | 3,107 | 4 |
| Return on equity [%] | 3.18 | 2.57 | 0.61 |
| Earnings per share [Rs.] | 0.61 | 0.47 | 29 |

Strategy for 2017

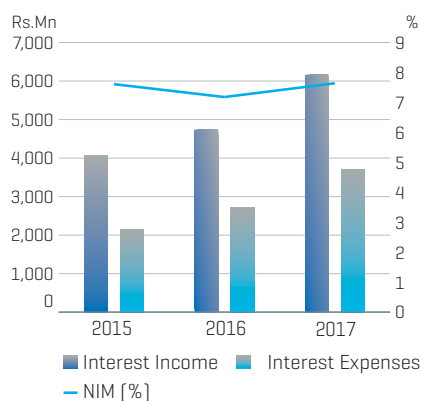
- Focus on strengthening credit fundamentals
- Cost rationalisation
- Redemption of high-cost deposits

Income Statement Analysis

Interest income

The Company's interest income growth was strong at 30%, supported by a credit portfolio expansion of 6% and increased investments in government securities and fixed deposits. The rising interest rate scenario inserted pressure on the Company's funding costs and interest expenses for the year increased by 37% during the year. Resultantly, net interest income growth of 21% was relatively slower than the Company's top line growth. Although net interest margins were impacted by the higher funding costs, the Company adopted timely measures to reprise its lending portfolio thereby enabling NIMs to be maintained at 7.64%. NIMs were also supported by the Company's higher exposure to the relatively high-yielding gold loan segment and redemption of high cost deposits during the year.

Income Statement Analysis



Other income

The Company's other income consists primarily of fee and commission income, trading income and insurance premium income. The Company's other income consists primarily documentation and other charges of lending facilities and commission income. The net fee and commission income of the Company increased by 28% reflecting the increased documentation and other charges in lending facilities granted during the year. The temporary halting of MBSL Insurance's operations also resulted in insurance premium falling by 44%

compared to last year. Net trading losses for the year amounted to Rs. 16.02 million as the Company sought to shed its equity investment portfolio. Supported by the expansion in interest income, the Company's operating income increased by 23% to Rs. 2.63 billion during the year under review.

Impairment on loans and advances

Impairment charges on loans and advances saw a significant increase during the year, rising to Rs.244.23 million from Rs. 24.24 million in 2016. The weakening credit quality reflects moderating economic conditions, a weaker agriculture sector as well as relatively lax credit practices adopted in the recent past. However, we have taken necessary steps to stem this deterioration, placing emphasis on strengthening credit fundamentals to achieve a sustainable improvement in credit quality.

Financial Capital

Initiatives undertaken to enhance underlying credit quality

- Discontinue loan products giving rise to high delinquencies, particularly unsecured loans
- Adopted a collateral-based approach to lending
- Streamlined recovery mechanisms
- Introduced a comprehensive credit inspection report
- Intense staff training

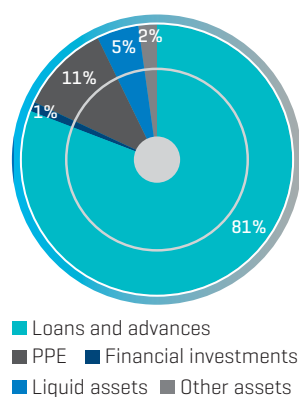
Cost Management

Overhead costs increased by 25% during the year reflecting higher personnel expenses, which is the largest component of overhead costs. Personnel expenses increased by 31% during the year following the signing of the collective agreement. The increase in other expenses (consisting of retirement benefits, depreciation and amortisation and other operating expenses) was contained at 16%. A cost awareness and rationalisation culture has been brought in and is gradually being nurtured across the organisation. The Company's cost to income ratio increased marginally to 73.10%, from 71.90% the year before.

Profitability

The Company's operating profit decreased by 20% to Rs.464.24 million during the year, reflecting higher impairment costs. The increase in the VAT rate applicable on financial services resulted in VAT escalating by over 61% during the year. Resultantly, the Company's pre-tax profits remained relatively unchanged compared to last year, clocking in at Rs. 228.65 million in 2017.

Balance Sheet Analysis

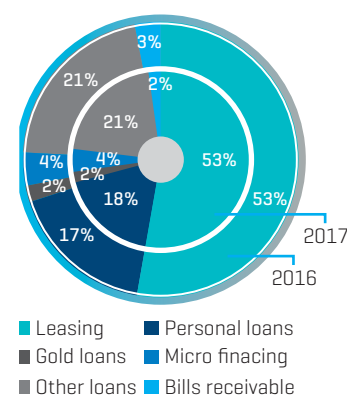


Total assets grew by 12% during the year to reach Rs.35.65 billion, supported by growth in advances of 6% and increased exposure to repurchase agreements, fixed deposits and unit trusts. As the Company sought consolidation in its loan book, the relatively moderate loan expansion during the year resulted in funds raised through debentures and securitisation being channelled towards fixed deposits and government securities. Accordingly, credit assets accounted for a reduced 81% of total assets as at end-December 2017, compared to 85% in 2016.

Financial Investments Portfolio

| | 2017 | 2016 |
|--|-------|-------|
| Resale agreements (Rs.Mn) | 1,303 | 266 |
| Quoted equities and unit trusts (Rs.Mn) | 227 | 321 |
| Debt securities (Rs.Mn) | 5 | 2 |
| Government securities-available-for-sale (Rs.Mn) | 641 | 2,694 |
| Unquoted investments (Rs.Mn) | 52 | 41 |
| Unit trust (Rs.Mn) | 1,123 | - |
| Held-to-maturity-treasury bonds (Rs.Mn) | 479 | 58 |

Loan Composition



The Company adopted a somewhat conservative approach to lending during the year, as focus was on consolidating our portfolio and strengthening the underlying credit quality. Leasing advances accounted for 54% of the Company's total portfolio and increased by 4% during the year upheld by the entry into the two and three-wheeler segment. In other loans, the Company pursued strong growth in the pawning segment, which saw advances increasing by nearly 40%. Term loans and personal loans also expanded by 7.35% and 13.70% respectively during the year under review. As discussed previously, credit quality deteriorated during the year and the Company's gross NPL ratio clocked in at 12.06%, from 11.48% the year before.

The operations of the Company's insurance associate, MBSL Insurance was temporarily halted due to inadequate capital. Although previously the Company had intended to dispose its entire stake in MBSL Insurance, the Board is of the view that the insurance industry presents ample opportunities for growth given the relatively low penetration levels in Sri Lanka. MBSL therefore intends to retain and revive the Company in partnership with a significant minority equity partner. Expressions of Interest (EOI) have already been called with several positive responses. A collective capital

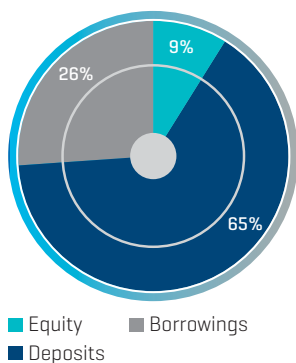
infusion to the tune of Rs.1.2 billion is expected over the short to medium term.

The funding strategy for the year centered on redeeming high-cost deposits and reducing the Company's average cost of funding. We successfully issued Rs.2.0 billion of unsecured, redeemable, subordinated debentures and raised Rs. 2.0 billion through securitisation. Deposits accounted for 65% of the Company's funding composition and grew by 18% during the year, attesting to the improving strength of MBSL's deposit franchise. Savings deposits also increased by 19% during the year, as we leveraged on our brand reputation and good track record. Exposure to borrowings remained relatively unchanged with total borrowings amounting to Rs.8.82 billion as at end-December 2017.

FORWARD OUTLOOK

The Company intends to achieve growth in its portfolio through focusing on gold loans, two and three-wheeler financing in 2018. Continued emphasis will be placed on maintaining strong credit practices to ensure that credit quality is maintained in parallel to portfolio growth. Capitalisation is strong following the issuance of a subordinated debenture in 2017 and has afforded us a strong platform for growth.

Funding Composition



Capital strength

The equity base increased by 4.0% to Rs. 3.26 billion supported by profit retention during the year. The tier 1 and overall Risk Weighted Capital Adequacy Ratios (RWCAR) clocked in at 10.21% and 15.27% as at end-December 2017, comfortably above the regulatory minimums and affording the Company ample opportunity for growth.

Financial Capital

Shareholder Value Creation

The Company is committed to generating sustainable shareholder returns, as demonstrated by the consistent growth of its earnings and net asset value per share. During the year the Company's EPS strengthened to Rs. 0.61 from Rs. 0.47 the year before while net asset value per share also increased by 4%. The share price declined marginally in view of the weak broad market conditions and is currently trading below its net asset value, demonstrating the value to be unlocked.

Public Holdings

| | 2017 | | 2016 | |
|----------------------------|---------------|--------------|---------------|--------------|
| | No. of shares | % of holding | No. of shares | % of holding |
| Shares held by the public | 42,307,029 | 25.51% | 42,302,815 | 25.50% |
| No. of public shareholders | 11,212 | 99.94% | 11,427 | 99.94% |

Foreign shareholding continued to be minimal, with 99.35% of shares held by residents

Distribution of Ordinary Shareholders

| | As at 31 December 2017 | | | | As at 31 December 2016 | | | |
|----------------------|------------------------|-----------------------|---------------|-----------------|------------------------|-----------------------|---------------|-----------------|
| | No. of shareholders | No. of shareholders % | No. of shares | No. of shares % | No. of shareholders | No. of shareholders % | No. of shares | No. of shares % |
| 1 To 1,000 | 9,159 | 81.64% | 1,626,774 | 0.98% | 9,286 | 81.21% | 1,690,172 | 1.02% |
| 1,001 To 10,000 | 1,640 | 14.62% | 5,769,648 | 3.48% | 1,734 | 15.17% | 6,037,485 | 3.64% |
| 10,001 To 100,000 | 369 | 3.29% | 10,809,941 | 6.52% | 363 | 3.17% | 10,050,987 | 6.06% |
| 100,001 To 1,000,000 | 48 | 0.43% | 12,213,580 | 7.36% | 48 | 0.42% | 11,104,996 | 6.69% |
| over 1,000,000 | 3 | 0.03% | 135,454,598 | 81.66% | 3 | 0.03% | 136,990,901 | 82.59% |
| Total | 11,219 | 100.00% | 165,874,541 | 100.00% | 11,434 | 100.00% | 165,874,541 | 100.00% |

Composition of Ordinary Shareholders

| | As at 31 December 2017 | | | | As at 31 December 2016 | | | | |
|--------------|------------------------|-----------------------|---------------|-----------------|------------------------|-----------------------|---------------|-----------------|---------|
| | No. of shareholders | No. of shareholders % | No. of shares | No. of shares % | No. of shareholders | No. of shareholders % | No. of shares | No. of shares % | |
| Resident | Individual | 10,224 | 91.13% | 20,720,562 | 12.49% | 10,427 | 91.19% | 19,785,711 | 11.93% |
| | Company | 944 | 8.41% | 143,131,142 | 86.29% | 955 | 8.35% | 145,015,408 | 87.42% |
| Non Resident | Individual | 49 | 0.44% | 905,039 | 0.55% | 50 | 0.44% | 905,939 | 0.55% |
| | Company | 2 | 0.02% | 1,117,798 | 0.67% | 2 | 0.02% | 167,483 | 0.10% |
| Total | | 11,219 | 100.00% | 165,874,541 | 100.00% | 11,434 | 100.00% | 165,874,541 | 100.00% |

Directors' Shareholding

| Names Of Directors | No. of shares | As a % of total shares | No. of shares | As a % of total shares |
|-----------------------|---------------|------------------------|---------------|------------------------|
| | 31.12.2017 | | 31.12.2016 | |
| Mr. C. N. Wijewardana | - | - | 4,235 | 0.003% |

CEO's Shareholding

| Name CEO | No. of shares | As a % of total shares | No. of shares | As a % of total shares |
|----------------------------|---------------|------------------------|---------------|------------------------|
| | 31.12.2017 | | 31.12.2016 | |
| Mr. D. M. N. P. Karunapala | 21 | 0.00001% | 21 | 0.00001% |

Market Share Information

| | 2017 | Q4 | Q3 | Q2 | Q1 | 2016 |
|--|-------|-------|-------|-------|-------|-------|
| Share price [Rs.] | | | | | | |
| Highest | 15.40 | 14.00 | 15.40 | 15.40 | 14.00 | 16.50 |
| lowest | 10.60 | 12.70 | 13.40 | 11.00 | 10.60 | 10.10 |
| Closing | 13.50 | 13.50 | 15.10 | 14.90 | 10.80 | 13.60 |
| No. of transactions | 4,570 | 1,203 | 979 | 1,886 | 502 | 4,392 |
| No. of shares traded [Rs. Mn] | 15.73 | 3.28 | 3.97 | 7.84 | 0.64 | 8.41 |
| Shares traded to total shares [%] | 9.5 | 2.0 | 2.4 | 4.7 | 0.4 | 5.1 |
| Turnover [Rs. Mn] | 224 | 48 | 58 | 110 | 8 | 119 |
| MBSL total turnover to total market turnover [%] | 0.10 | 0.09 | 0.11 | 0.17 | 0.02 | 0.07 |
| No. of days traded | 241 | 60 | 62 | 57 | 62 | 234 |
| Average daily turnover - CSE [Rs. Mn] | 915 | 917 | 888 | 1,140 | 735 | 738 |
| Market Capitalisation - CSE [MC][Rs. Bn] | 2,899 | 2,899 | 2,920 | 3,041 | 2,663 | 2,745 |
| Market Capitalisation - MBSL [MC][Rs. Bn] | 2.20 | 2.20 | 2.50 | 2.47 | 1.79 | 2.25 |
| MBSL MC to CSE MC [%] | 0.08 | 0.08 | 0.09 | 0.08 | 0.07 | 0.08 |
| MBSL market capitalisation ranking | 146 | 146 | 140 | 145 | 153 | 135 |

Twenty Largest Shareholders

| | As at 31 December 2017 | | | As at 31 December 2016 | |
|---|------------------------|------------------------|-----------------------------------|------------------------|------------------------|
| | Number of shares | Percentage holding [%] | Cumulative percentage holding [%] | Number of shares | Percentage holding [%] |
| 1 Bank Of Ceylon No. 1 Account | 123,562,267 | 74.49% | - | 123,562,267 | 74.49% |
| 2 Bank Of Ceylon A/C Ceybank Unit Trust | 10,788,183 | 6.50% | 81.00% | 10,796,141 | 6.51% |
| 3 Sandwave Limited | 1,104,148 | 0.67% | 81.66% | - | - |
| 4 Mr. M.M. Fuad | 841,837 | 0.51% | 82.17% | 310,114 | 0.19% |
| 5 People's Leasing & Finance PLC / Mr.D.M.P.Disanayake | 632,485 | 0.38% | 82.55% | 428,450 | 0.26% |
| 6 Richard Peiris Financial Services (Pvt) Ltd / M.A.A.Karim | 578,109 | 0.35% | 82.90% | 556,651 | 0.34% |
| 7 Merrill J Fernando & Sons (Pvt) Limited | 526,165 | 0.32% | 83.22% | 526,165 | 0.32% |
| 8 Seylan Bank PLC/Spice of Life (Pvt) Ltd | 405,234 | 0.24% | 83.46% | 387,934 | 0.23% |
| 9 Mr. K.V. Hewavitarne | 400,000 | 0.24% | 83.70% | - | - |
| 10 Hatton National Bank PLC / Dinesh Nagendra Sellamuttu | 386,301 | 0.23% | 83.93% | 386,301 | 0.23% |
| 11 Mr. N. Balasingam | 381,400 | 0.23% | 84.16% | 381,400 | 0.23% |
| 12 Seylan Bank Plc/Ms.Prime Lands (Pvt) Ltd | 375,000 | 0.23% | 84.39% | 375,000 | 0.23% |
| 13 Mrs. F.F. Hanifa | 352,481 | 0.21% | 84.60% | 225,000 | 0.14% |
| 14 Mr. B.T. Prathapasinghe | 345,000 | 0.21% | 84.81% | 345,000 | 0.21% |
| 15 Mr. A. Chelliah[Deceased] | 333,800 | 0.20% | 85.01% | 333,800 | 0.20% |
| 16 Mr. A.M. Weerasinghe | 305,583 | 0.18% | 85.20% | 305,583 | 0.18% |
| 17 Bartleet Produce Marketing (Pvt) Limited | 300,000 | 0.18% | 85.38% | 300,000 | 0.18% |
| 17 People's Leasing & Finance PLC / L.P.Hapangama | 300,000 | 0.18% | 85.56% | 300,000 | 0.18% |
| 19 Mrs. H.M. Hettiarachchi | 294,858 | 0.18% | 85.74% | - | - |
| 20 Mr. W.L.T. Anandawansa | 282,039 | 0.17% | 85.91% | 282,039 | 0.17% |
| Total of largest shareholders | 142,494,890 | 85.91% | | | |
| Total of other shareholders | 23,379,651 | 14.09% | | | |
| Total of all shareholders | 165,874,541 | 100.00% | | | |

Financial Capital

Debenture Information

Debenture - Market Information

| 2017 | | | | | | | | |
|--|-----------------------------|---------------|---------------|-----------------------------|---------------------|-----------------------------|---------------------|---------------------|
| Type | Type A 13 Mar | Type C 13 Mar | Type D 13 Mar | Type A 14 Nov | Type B 14 Nov | Type A 17 May | Type B 17 May | Type C 17 May |
| Tenure | 5 Years | 5 Years | 5 Years | 5 Years | 5 Years | 5 Years | 5 Years | 5 Years |
| Issue date | 28-Mar-13 | 28-Mar-13 | 28-Mar-13 | 13-Nov-14 | 13-Nov-14 | 12-May-17 | 12-May-17 | 12-May-17 |
| Maturity date | 27-Mar-18 | 27-Mar-18 | 27-Mar-18 | 12-Nov-19 | 12-Nov-19 | 3-May-22 | 3-May-22 | 3-May-22 |
| Interest rate | 17.50% | 16.70% | 16.50% | 9.00% | 8.75% | 15.00% | 14.50% | 12.11% |
| Coupon rate | 17.50% | 16.70% | 16.50% | 9.00% | 8.75% | 15.00% | 14.50% | 12.11% |
| Effective annual yield | 17.50% | 17.78% | 17.81% | 9.00% | 8.94% | 15.00% | 15.03% | 12.48% |
| Interest rate comparable government security | 11.56% | 11.56% | 11.56% | 11.94% | 11.94% | 10.20% | 10.20% | 10.20% |
| Frequency of interest payable | Annually | Quarterly | Monthly | Annually | Bi - annually | Annually | Bi - annually | Bi - annually |
| Rating | A : By ICRA [Lanka] Limited | | | A : By ICRA [Lanka] Limited | | A : By ICRA [Lanka] Limited | | |
| Amount [Rs. Mn] | 625.11 | 723.19 | 166.46 | 909.77 | 1,090.23 | 805.76 | 1,193.23 | 1.01 |
| ISIN No. | LK0186019194 | LK0186019210 | LK0186019228 | LK0186022669 | LK0186022677 | LK0186023824 | LK0186023816 | LK0186023808 |
| Highest | 107.92 | 101.47 | 100.31 | | | | | |
| Lowest | 101.73 | 101.47 | 100.30 | | | | | |
| Closing | 101.73 | 101.47 | 100.30 | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED |
| Current yield | 17.20% | 16.46% | 16.45% | | | | | |
| YTM | 16.96% | 16.25% | 16.41% | | | | | |

| 2016 | | | | | | | | |
|-----------------------------|---------------|---------------|---------------|-----------------------------|---------------------|---------------------|-----------------------------|---------------------|
| Type A 13 Mar | Type B 13 Mar | Type C 13 Mar | Type D 13 Mar | Type A 13 Dec | Type C 13 Dec | Type D 13 Dec | Type A 14 Nov | Type B 14 Nov |
| 5 Years | 4 Years | 5 Years | 5 Years | 4 Years | 4 Years | 4 Years | 5 Years | 5 Years |
| 28-Mar-13 | 28-Mar-13 | 28-Mar-13 | 28-Mar-13 | 17-Dec-13 | 17-Dec-13 | 17-Dec-13 | 13-Nov-14 | 13-Nov-14 |
| 27-Mar-18 | 27-Mar-17 | 27-Mar-18 | 27-Mar-18 | 16-Dec-17 | 16-Dec-17 | 16-Dec-17 | 12-Nov-19 | 12-Nov-19 |
| 17.50% | 17.25% | 16.70% | 16.50% | 14.25% | 13.50% | 13.25% | 9.00% | 8.75% |
| 17.50% | 17.25% | 16.70% | 16.50% | 14.25% | 13.50% | 13.25% | 9.00% | 8.75% |
| 17.50% | 17.25% | 17.77% | 17.80% | 14.25% | 14.20% | 14.09% | 9.00% | 8.94% |
| 11.56% | 11.56% | 11.56% | 11.56% | 10.31% | 10.31% | 10.31% | 11.94% | 11.94% |
| Annually | Annually | Quarterly | Monthly | Annually | Quarterly | Monthly | Annually | Bi - annually |
| A : By ICRA [Lanka] Limited | | | | AA: By ICRA [Lanka] Limited | | | A : By ICRA [Lanka] Limited | |
| 625.11 | 485.24 | 723.19 | 166.46 | 674.77 | 17.54 | 11.47 | 909.77 | 1,090.23 |
| LK0186D19194 | LK0186D19202 | LK0186D19210 | LK0186D19228 | LK0186D20929 | LK0186D20911 | LK0186D20937 | LK0186D22669 | LK0186D22677 |
| 115.18 | 102.56 | 102.00 | 101.00 | 102.63 | | | | |
| 107.92 | 102.56 | 102.00 | 101.00 | 102.62 | | | | |
| 115.18 | 102.56 | 102.00 | 101.00 | 102.62 | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED | HAS NOT BEEN TRADED |
| 15.19% | 16.82% | 16.37% | 16.34% | 13.89% | | | | |
| 13.16% | 16.33% | 15.95% | 16.19% | 13.36% | | | | |

Manufactured Capital



The year under review marked an important milestone for the Company, as it successfully implemented a state-of-the-art core banking platform. Over the medium to long-term this implementation is expected to facilitate the Company’s transition to an efficient, customer-centric organisation and provide management access to real-time, holistic information.

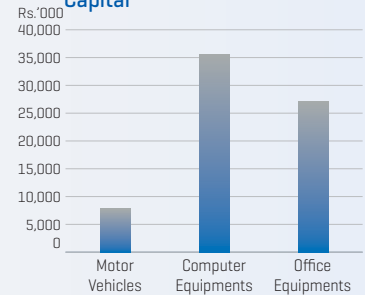
Highlights of 2017

| | 2017 | 2016 | y-o-y % |
|--|------|------|---------|
| Investment in Property and equipment (Rs.Mn) | 85 | 154 | (45.20) |
| Branches | 49 | 49 | 0 |
| Branch relocations | 05 | 04 | 25 |
| Investment in core banking platform (Rs.Mn) | 306 | - | - |

Strategy for 2017

- Successful implementation of core banking platform
- Introducing new products
- Revamping current branches to enhance customer experience

Value Addition to Manufactured Capital



Digital Infrastructure

The Company’s core banking system was implemented in July 2017 followed by a smooth migration to the new system. All employees were provided comprehensive training on the new system to ensure an effective transition with minimum disruptions to daily operations. Information security was also strengthened during the year with enhanced perimeter level security. Over the short term we intend to completely secure the second layer (the internal network) and the third layer (data centre).

The state-of-the-art system is expected to accrue numerous benefits for the organisation, including the following;

- Strengthen risk management through providing access to real time information
- Enable new product development and strengthen collection mechanisms
- Enhance the customers’ self service propositions such as ATMs, online and mobile banking
- Eliminate manual elements of financial reporting

Physical Infrastructure

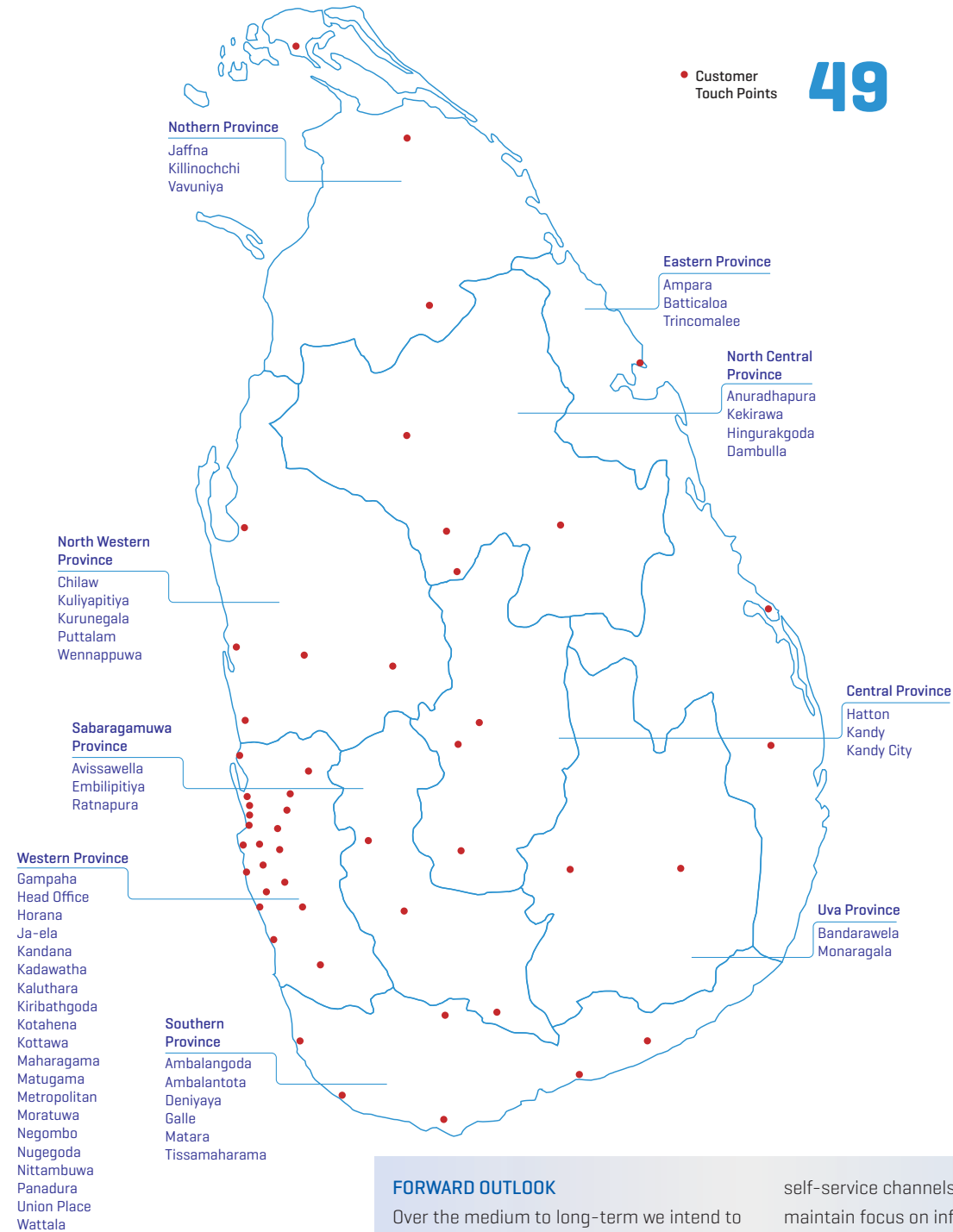
The Company’s physical infrastructure consists of 49 branches across 22 districts, which are the key contact points for customer engagement. Leasing as well as SME and retail products are promoted to customers through the branch network, facilitating both credit growth and deposit mobilization. Gold loan facilities are disbursed through 34 of these branches while the Company’s subsidiary, MBSL Insurance also operates a network of 34 branches. During the year we focused on consolidating our physical network and providing an enhanced customer experience through the existing network. Accordingly, we invested Rs. 16.91 million in revamping 03 branches with changes done to the layout, front-line processes and ambience to deliver an enhanced customer experience; this will be rolled out

across our entire network over the short-to-medium term to ensure consistency in the customer experience.

The island-wide branch network affords the Company a strong platform for growth and has enabled us to work towards our long-term objective of driving financial inclusion and increasing regional access to affordable funding. Of our network 04 branches are in economically underprivileged areas of the country.



Manufactured Capital



FORWARD OUTLOOK

Over the medium to long-term we intend to strengthen our customer digital proposition with the launch of online and mobile banking platforms which such as ATMs which will support our deposit growth. Following the implementation of the core-banking system, the platform is in place to enhance the customer experience through these

self-service channels. We will continue to maintain focus on information security, to ensure the smooth functioning of our operations as well as preserving customer information. Further expansion of the branch network is unlikely over the medium term, as focus will be placed on consolidating the existing network and driving profitable growth in all locations.

Human Capital



Our human capital consists of a loyal team of 968 employees who drive our culture, values, mission and goals. The skills, attitudes and capabilities of our team is vital in achieving our strategic ambitions and during the year, we placed emphasis on nurturing a performance-driven culture through significant investments in people development and employee engagement.

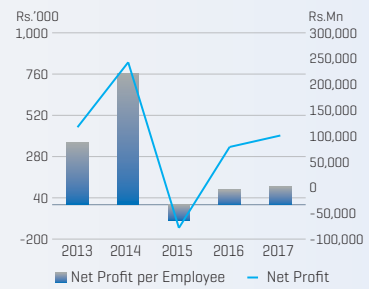
Highlights of 2017

| | 2017 | 2016 | y-o-y % |
|--------------------------------------|--------|--------|---------|
| Total employees | 968 | 917 | 6 |
| New recruits | 185 | 217 | (15) |
| Retention [%] | 89 | 85 | 4 |
| Female representation [%] | 38 | 38 | - |
| Total payments to employees [Rs. Mn] | 1,015 | 788 | 29 |
| Investment in training [Rs. Mn] | 10 | 15 | (33) |
| Training hours | 22,140 | 18,395 | 20 |
| Promotions | 109 | 10 | 990 |

Strategy for 2017

- Nurturing a performance-driven culture through intense training and development initiatives
- Enhancing the performance management system to drive increased productivity

Productivity



Approach and HR Governance

We adopt a structured and formalised approach towards HR governance with clearly defined roles and responsibilities and comprehensive policies. The policy framework has a broad coverage of multiple aspects pertaining to HR management including recruitment, equal opportunity, rewards and recognition, training and development, grievance mechanisms and industrial relations among others. The Board of Directors, supported by the HR and Remuneration Committee formulate the human capital strategy for the year and ensure effective implementation of the same. The HR Department drives the Board’s HR strategy and operates under the purview of the CEO.



Policy Framework

The policy framework forms an integral part of HR governance and ensures that employees are treated consistently and equitably. Several aspects related to talent attraction, development and retention have been covered by comprehensive policies. During the year, the company revised 02 policies.

| List of our policies | Description |
|-------------------------------|---|
| Recruitment Policy | Ensure concepts of diversity and equal opportunity are considered on recruitment of employees |
| Promotion Policy | Defines the parameters and pathways for promotion such as general and merit based All employees have been an equal career development opportunities based on their competency profiles and performance achievement under the stated policy |
| Grievance Policy | MBSL maintains an open- door policy and a structured grievance mechanism with defined roles and responsibilities for grievance handling |
| Training & Development Policy | Training needs are identified at performance appraisals and all employees are given access to internal as well as external training programs |



Focus areas in 2017

| Governance | Performance management | Culture | Development |
|--|--|---|---|
| During the year we reviewed and revised O2 policies. | Developed measurable KPIs in line with strategic priorities of 2017. Developed measurable KPIs in line with strategic business goals at year 2017. | Focused on creating a market driven and credit conscious culture. | Increased scope of learning interventions to cover change management, credit evaluation, recovery management, core banking [system training] and soft skills to cover credit appraisal, monitoring, IT and soft skills. |

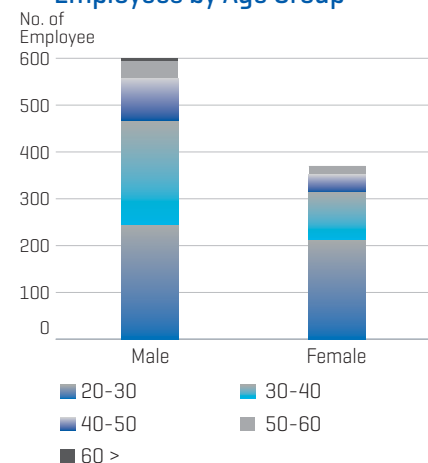
Our deliverables during the year

| KPIs | 2017 | 2016 | 2015 |
|--|--------|--------|--------|
| No of employees | 968 | 917 | 866 |
| Employee retention [%] | 89 | 85 | 83 |
| Cost of rewards and benefits as % of revenue | 16% | 16% | 16% |
| Revenue per employee | 6,614 | 5,330 | 4,870 |
| Avg No. of facilities handled/employee | 976 | 849 | 551 |
| Investment in training [Rs. Mn] | 10 | 15 | 7 |
| Training hours | 22,140 | 18,395 | 11,100 |

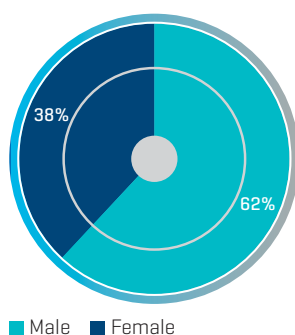
Team Profile

As an organisation, we value diversity and continue to maintain a team of employees who are diverse in their gender, age and skill representation. The employee cadre in 2017 was 968 in number and increased by 6% compared to last year in line with increasing operational requirements of branches. Our workforce is relatively young, with 46% of employees under the age of 30 and are more adaptable to change.

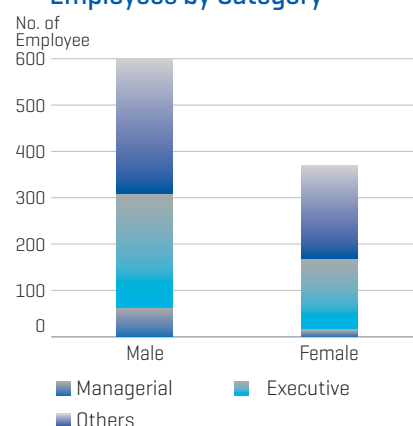
Employees by Age Group



Work Force by Gender



Employees by Category



Engagement

Continuous employee engagement supports performance monitoring and strengthens employer -employee relationships. It's a means of fostering commitment towards work as employees develop a sense of belongingness to the organization. During the year, both formal and informal channels were used to continuously connect with employees. Formal approaches include performance evaluation conducted periodically for all employees. This supported the organization in promptly addressing any employee staff performance achievement grievances, evaluating employee satisfaction and identifying competency gaps in the workforce. Routine forms of engagement include monthly staff meetings, face to

Human Capital

face meetings and ongoing social events. Additionally, other platforms such as intranet and corporate website enabled employees to be updated on the activities and progression of the organization. The minimum notice period provided to employees for operational changes are three months in the event of both retirements and terminations. The MBSL Welfare and Recreational Club aims to foster a team spirit and camaraderie among employees through a year-round event calendar. The club also provides financial assistance in the event of the death of a family member.

Other work life balance events held during the year include:

- **Poson Bathi Gee Saraniya**
In June 2017, MBSL organized the Poson Bathi Gee Saraniya with the participation of all employees including branch level staff.
- **MBSL Buon Natale**
MBSL's Annual Glamours Christmas Carols was held in December 2017 with the participation of all employees.



Freedom of Association

We are cognisant of employee rights to freedom of association and continue to maintain cordial relationships with the trade unions. Around 53% of our cadre is represented by the MBSL branch of the Ceylon Bank Employees Union. The Bank entered into a collective agreement with the union represented staff in January 2017. There were no disruptions such as freedom of association, child labour forced to work resulting from industrial disputes during the year.

Organisational Culture

During the year, we focused on several initiatives to drive a performance driven culture focused on sales, credit orientation and productivity. Training initiatives and employee engagement mechanisms were designed to drive workforce towards a performance driven culture. Measurable KPIs were shared across all business functions with progression being continuously monitored through management information systems. Additionally, employees were continuously updated on the progression of KPIs which enhanced awareness and commitment of employees towards organizational goals.

Training and Development

Training was a key strategic focus area during the year, with nearly 97% of our employees undergoing some form of training in 2017. The scope of the training programs were determined based on the organisation's strategic agenda and competency gaps identified at Annual Training Needed Analysis (TNA). In 2017 the training programs were categorised as technical behaviours system (Core banking). Focus areas included leadership development, change management, credit evaluation, recovery management, customer relationship, sales & marketing,

compliance management supported the development of a market driven, anti-corruption, risk conscious culture within our organization.

We placed particular emphasis on the sales level staff and in around 75% of the training hours were on employees below managerial levels. As an initiative to evaluate the effectiveness of training programs, employees were given the opportunity to provide their feedback on the programs. In addition to our ongoing training programs, we also provided internship opportunities to students following undergraduate courses and other professional qualifications. During the year, 30 interns were trained under approved training partner agreements.

| | 2017 | 2016 |
|--|--------|--------|
| Training hours | | |
| Core banking (system) hours | 9,144 | - |
| General training (technical behavioural) hours | 12,996 | 18,395 |
| Training hours | 22,140 | 18,395 |
| Training hours/employee | 24 | 21 |
| Number of employees | 939 | 917 |
| % of workforce | 99 | 100 |
| No of males | 599 | 571 |
| No of females | 369 | 346 |
| Training spend (Rs. Mn) | | |
| Training expenditure | 10 | 15 |
| Training expenditure per employee. (Rs.) | 16,520 | 10,650 |

Performance Management

We strengthened our performance management framework during the year, with measurable KPIs being deposit growth, lending growth, contribution, profitability, PA introduced in line with organisational

strategic objectives. Performance targets in 2017 focused on profitable growth, credit quality and recoveries. Credit recovery targets were set to strengthen the credit process and increase collections from existing clientele.

Routine performance evaluations centred on key performance indicators and supported proactive identification of skill gaps.

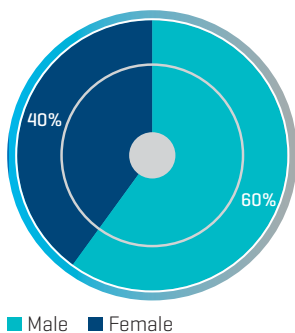
Career Development

All employees have given equal career development opportunity to apply for the annual promotion process under the general and merit promotion channels. Accordingly, 109 employees were promoted during the year 2017.

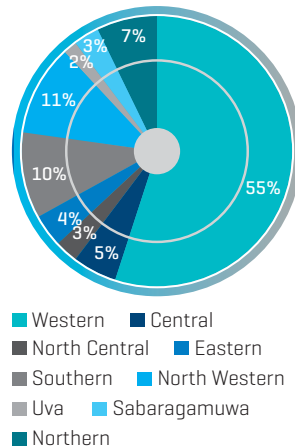
Attracting Talent

Effective recruitment plays an integral role in our business operations and we strive to recruit the best talent available. During the year, 185 new employees joined our workforce. As part of our policies, local communities continued to be an important channel for recruitment with 73% of recruitments being within the vicinity of branches. This enabled our cadre to be diversified across nine provinces in the country with the Western province accounting for 55% of recruitments while other local communities represented the balance.

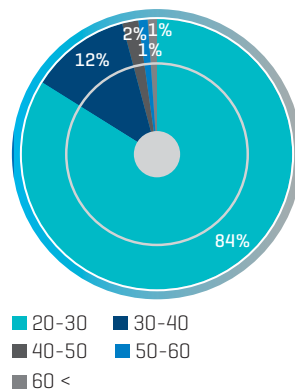
Recruits by Gender



Recruits by Region



Recruits by Age



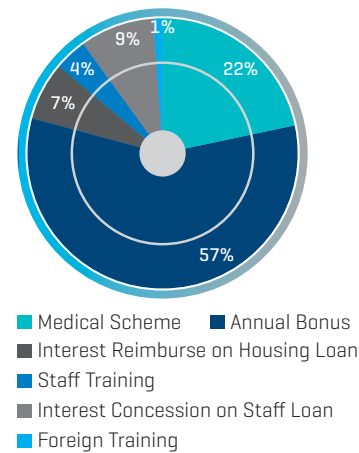
Talent Retention

The Company's retention rate is relatively good at nearly 89%, supported by attractive remuneration schemes and the conducive culture. We are an equal opportunity employer, and do not discriminate between gender, age or other measures of diversity in recruiting or remunerating employees. We maintained 1:1 salary ratio between males and females.

Retirement plans in the form of pension contributions and gratuity payments form a source of retirement income for our employees. We contributed 12% and 3%

to the Employee Provident Fund (EPF) and Employee Trust Fund (ETF) in addition to gratuity payments for all employees on the completion of five years.

Key Benefits & Costs

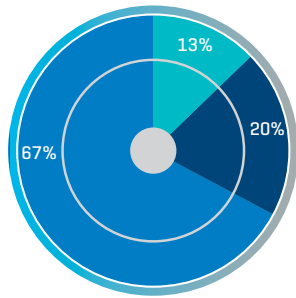


Other Benefits

1. Insurance
2. Medical scheme: enabling re-imbursement of hospitalization expenses of employees. Employees and their dependents could join the scheme on the payment of a token membership fee.
3. Maternity leave and Nursing intervals
4. Housing loan re-imbursements up to an entitlement limit of Rs. 4 Mn is provided to any employee on completion of 3.5 years of service.
5. Other loans such as car loans and personal loans for permanent employees.
6. Re-imbursement of exam fees

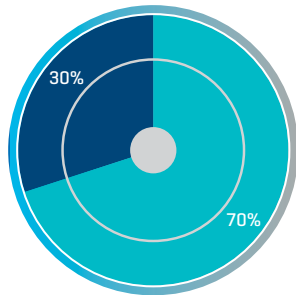
Human Capital

Exits by Grade



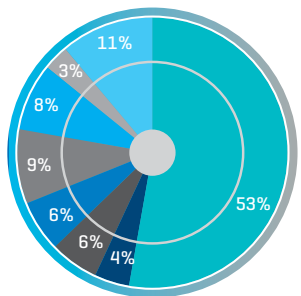
■ Managerial ■ Executive
■ Clerical & Support Staff

Exits by Gender



■ Male ■ Female

Exits by Region



■ Western ■ Central
■ North Central ■ Eastern
■ Southern ■ North Westerr
■ Uva ■ Northern

| | 2017 | 2016 |
|---|------|------|
| No of female employees | 369 | 346 |
| No of employee who took maternity leave | 25 | 16 |
| Return to work after maternity leave | 24 | 13 |
| Return to work rate | 96% | 81% |

FORWARD OUTLOOK

Going forward, our focus remains on transforming the organizational culture to one that is market driven and risk conscious. This will support the strategic re-alignment initiated during the year giving prominence to loan quality, customer growth and credit recovery. A learning culture will continue to play a prominent role in developing employees and intense training programmes will be conducted to ensure that employees are equipped with the skills required to drive the Company's strategic aspirations.

Intellectual Capital



The Company's Intellectual Capital is represented by organisational tacit knowledge, systems process and protocols which define the way we work and the value of our brand. Our intellectual capital has been nurtured over our track record exceeding 35 years and has enabled us to build sustainable relationships with our customers and other stakeholders.

Highlights of 2017

| | 2017 | 2016 | y-o-y % |
|----------------------------------|------|------|---------|
| Brand value* (Rs. Mn) | 774 | 475 | 63 |
| Brand ranking among corporate | 58 | 76 | [24] |

*LMD and Brand Finance 2017

Strategy for 2017

- Targeted marketing and promotional campaigns
- Ongoing social media engagement with stakeholders
- Continued focus on upholding our corporate values in all aspects of our business

Corporate Values

The Company's corporate values define the principles that underpin our internal conduct and stakeholder interactions. These are the essence of our organisational entity and play an important role in shaping our culture and employee behaviour. The values are communicated to employees during recruitment and reinforced through subsequent engagement mechanisms.

Uphold the highest traditions of ethics, norms and best practices in all our endeavors

Guide our principles with wisdom and prudence in search of excellence

Foster intrapreneurship among our employees in creating an atmosphere of caring, sharing and integrity

Ensure good governance and transparency

Delight our clientele through service excellence, differentiation and innovation

Unite and be courageous to face challenges

Systems and Processes

MBSL has developed a suite of policies, structures, systems and processes which define the responsibilities and outlines the principles in daily operations and decision making. The policies are reviewed and revised regularly to reflect changes in our strategy as well as emerging risks and opportunities. These structures also play a vital role in preserving the Company's reputation and risk profile.

Intellectual Capital

Policy Frameworks

| HR | Risk Management | Operations | Information Technology |
|---|--|--|--|
| <ul style="list-style-type: none"> Recruitment Promotion Grievance Training & Development | <ul style="list-style-type: none"> Risk Management Liquidity Risk Management | <ul style="list-style-type: none"> Credit Savings accounts Investment Compliance Treasury management Pawn broking Real estate Branch, Region & Range Operation | <ul style="list-style-type: none"> Information Security Asset Management Human Resources Security Physical and Environmental Security Operations Security Management Communications Security Management Access Control Policy Systems Acquisition, Development & Maintenance Third Party Relationships Management Information Security Incident Management E-mail Security Policy on Information Security aspects of Business Continuity Management Bring Your Own Device Internet and Social Media Compliance |

International Europe Award for Quality 2017- Global Trade Leaders' Club, Paris

Asia's Best Employer Brand 2017- World Human Resource Development Congress

Emerging Financial Institute of the year 2017- Middle East Asia Leadership Summit



Brand

Ongoing efforts are in place to enhance MBSL's brand reputation among its target markets and during the year focus was placed on achieving deeper penetration in the two and three-wheeler leasing segment through targeted marketing campaigns and print/social media. In 2017, MBSL was ranked among Sri Lanka's top 10 consumer finance service brands by LMD and Brand Finance, attesting to it's position as a fast-growing, customer-oriented entity. In addition to the 7th position in the consumer service brands, the Company was also ranked among the country's top 100 corporates, with its position improving from 76 to 58 within the course of the year.

Ranked among the country's top 100 corporates with a brand value of Rs. 774 million

Awards

MBSL is frequent recipient of local and international awards and accolades, providing external assurance to stakeholders regarding the robustness of our operations and practices. Awards received in recent years include, but are not limited to the following;

Ranked No. 7 in the Consumer Finance Services sector



Social and Relationship Capital



As an organisation, we understand the importance of being attuned to the needs of our stakeholders and proactively responding to their concerns. This approach has been fundamental in creating and sustaining our value creation efforts and driving meaningful change.

Highlights of 2017

| | 2017 | 2016 | y-o-y % |
|--|---------|---------|---------|
| No. of lending customers | 72,489 | 70,864 | 2 |
| No. of fixed deposit customers | 6,002 | 5,290 | 13 |
| No. of savings customers | 144,171 | 120,065 | 20 |
| Customers outside the Western Province [%] | 57 | 58 | 1 |
| No. of suppliers | 134 | 130 | 3 |
| Payments to suppliers [Rs. Mn] | 372 | 348 | 7 |
| Investment in CSR [Rs. Mn] | 2.55 | 0.47 | 449 |

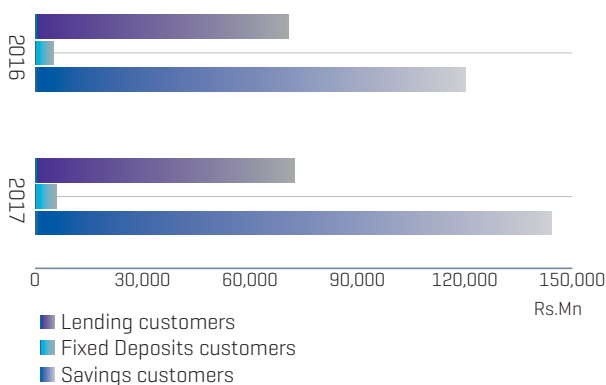
Strategy for 2017

- Customer acquisition in lending segments such as two and three-wheeler financing
- Focus on enhancing customer experience through branch upgrades and relocations
- Ongoing investment in community engagement initiatives

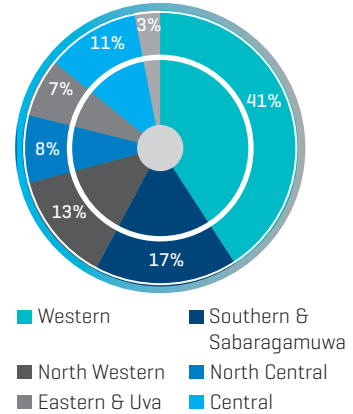
Customer Relationships

Our customers are an integral part of our value creation agenda, and we cater to 72,489 individual, corporate and SME lending customers across the island, through a holistic value proposition aimed at supporting customer requirements through different stages of business and personal growth. In 2017, following aggressive promotions and marketing campaigns we added 40,491 new facilities to our base. We also serve over 148,000 deposit customers through a range of attractive fixed and savings deposit products. Customers also vary in terms of their industry exposure, representing agriculture, fisheries, dairy, and cottage industries among others.

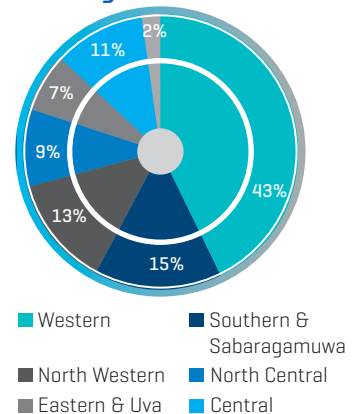
Customer Profile



Regional Breakdown of Lending Portfolio-2017



Regional Breakdown of Bending Portfolio-2016



Social and Relationship Capital

Customer Engagement

We have nurtured long-term relationships with our customers, facilitated through a high level of engagement through numerous platforms. MBSL conducts customer surveys, face to face interactions, a customer hotline and also engages in multiple forms of print and electronic media communication, including the interactive corporate website and social media platforms including Facebook and LinkedIn. The feedback obtained from these engagement mechanisms are a key input to our marketing, customer service and product development strategies. In 2017, we further strengthened our customer engagement through implementing a formal customer complaint handling process applicable to all branches.

Social Media Engagement

With a view to increasing brand recognition and engagement among millennials, MBSL has continued to enhance its social media presence during the year. The Company's Facebook page features exciting offers, product details and other information relevant for potential and existing customers. By end-2017, total 'likes' on our page exceeded more than 7,250.

Membership of Associations

- The Institute of Bankers of Sri Lanka
- The Institute of Chartered Accountants of Sri Lanka
- Central Bank of Sri Lanka
- Colombo Stock Exchange
- Securities and Exchange Commission of Sri Lanka
- Leasing Association of Sri Lanka
- Ceylon Chamber of Commerce
- The Credit Information Bureau of Sri Lanka
- The Department of Registrar of Companies
- Ministry of Public Enterprise Development

- Sri Lanka Accounting and Auditing Standards Monitoring Board

Customer Accessibility

Following an aggressive branch roll-out a few years ago, and the amalgamation in 2015, MBSL currently operates a network of 49 branches in all 9 provinces of the country. Our customers are also able to obtain a limited range of our services such as loan repayments, cash & cheque deposits & slip account transfers through our parent's extensive branch reach, which consists of nearly 600 island-wide branches. Following the successful implementation of the core banking system, the Company now has a strong platform to launch self-service channels including online and mobile banking platforms, which it intends to do over the medium to long-term.

| Provinces | No of Branches |
|---------------|----------------|
| Southern | 6 |
| Eastern | 4 |
| North Central | 5 |
| Western | 20 |
| Uva | 2 |
| North Western | 4 |
| Central | 4 |
| Sabaragamuwa | 2 |
| Northern | 2 |

Customer Experience

In 2017, we placed strategic focus on enhancing the customer experience through launching a branch upgrade campaign. We invested Rs. 16.91 million in revamping 3 branches with changes done to the layout, front-line processes and ambience to deliver an enhanced customer experience. The branches thus upgraded were Matara, Kurunegala and Gampaha. This initiative will be rolled out across our entire network over the short-to-medium term to ensure consistency in the customer experience.

Responsible Lending

We ensure that the terms and conditions applicable to our products and services are clearly understood by all customers. Relevant information such as interest rates on loans and deposits, and other terms are clearly communicated to all customers. Detailed product brochures which comply with CBSL requirements and other relevant legislation are made available to all customers. Marketing officers and Relationship managers are also responsible for explaining product characteristics, cost structures, benefits and any other relevant information to potential and existing customers. During the year, there were no instances of non-compliance to any relevant product and service related regulation or other guidelines.

Meanwhile, the Company's marketing communications follow a structured approval process to ensure compliance to accuracy, relevant regulatory requirements and consistency to our branding guidelines. During the year, there were no incidents of non-compliance to any regulations, voluntary codes or other guidelines pertaining to marketing communications.

Preserving Customer Privacy

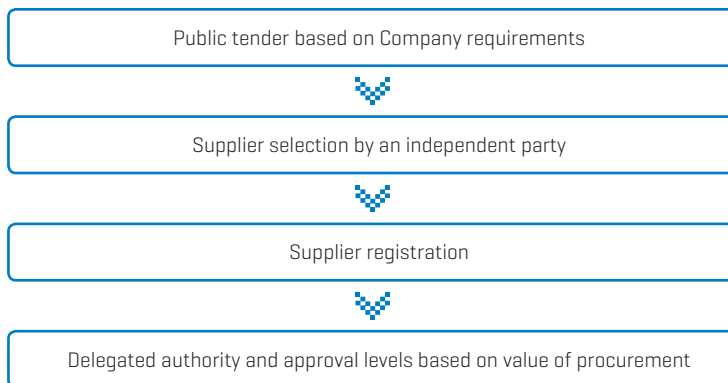
As a financial institution, we understand the important obligation we have towards preserving the financial and personal information of our customers. Following the implementation of the core banking system, we further strengthened our information security framework during the year by enhancing perimeter level security. An IT Security Council is also in place within the Company, which regularly reviews the required improvements in information security measures. We have also introduced robust access control measures and operate a disaster recovery site with real time data backup. During the year there were no incidents of non-compliance to any regulations, voluntary codes pertaining to customer privacy.

Suppliers and Business Partners

MBSL procures products and services from numerous parties, ranging from material suppliers to utility service providers and asset suppliers approximately 50% of the Company’s procurement spending is on local suppliers. The Company’s supply chain is illustrated in the infographic below.



Following the implementation of the 19th Amendment, the Company’s procurement is now governed by the Government’s National Procurement Guidelines, which emphasises the importance of cost-effective procurement. At MBSL, dedicated Procurement Committee is also in place to ensure the effective implementation of the stipulations set out in the manual. Public tenders are called annually, and supplier selection is done carried out entirely by an independent third party, ensuring the integrity of the process. Selected new suppliers are registered on a central database.



Community Engagement [Corporate Social Responsibility]

The community relationships we have nurtured over the years provide us the social license to operate and enable us to generate sustainable value to the communities we operate in. The Board of Directors hold apex responsibility for ensuring that all community engagement initiatives carried out by the Company are broadly in line with its sustainability objectives. The responsibility of selecting, effectively implementing and monitoring the performance of these projects lies with the corporate management team. Key CSR activities conducted on an ongoing basis and/or carried out as a one-off initiative during the year are given below;

Developing Entrepreneurship

Our micro finance initiative, Siyath Saviya combines our business objectives with our sustainability agenda in providing financial support to rural entrepreneurs who have limited access to other avenues of funding due to their risk profile. Under this program we provide collateral free loans to individuals engaging in agriculture, small businesses and dairy production. The initiative has been designed to primarily benefit vulnerable groups, including women and entrepreneurs in the North Central and Eastern provinces of the country. Since inception in 2010 we have supported the livelihoods of nearly 24,000 entrepreneurs through financial assistance, technical support and other forms of guidance. The Siyath Saviya initiative has directly benefitted these communities through,



Social and Relationship Capital

Female empowerment

Provide an additional source of income to underprivileged families

Contribute towards the socio-economic progress of families

Refurbishment of Gynaecology Unit at the National Hospital of Colombo

During the year, MBSL invested Rs. 0.3 Mn in refurbishing the 39th ward of Gynaecology Unit at the National Hospital of Colombo. In addition to the provision of patient care, the Unit also supports the training requirements of medical students and postgraduate doctors. Services provided at the unit include elective and emergency surgeries and managing female reproduction disorders. At an investment of Rs.0.3 Mn, this initiative has directly resulted in an improvement in general administration functions, enhancing quality of patient care and improving the standards of teaching for students.

Maintenance of flower troughs at Viharamahadevi Park

MBSL sponsors the maintenance of 72 flower troughs facing the main road at the Viharamahadevi Park at an annual cost of Rs. 0.38 Mn. The sponsorship also serves as an opportunity for us to display our branding through 25 sign boards in the areas facing the main roads of the park.

Embilipitiya MBSL Vidu Piyasa Project

MBSL collaborated with the Army Air Mobile Brigade to establish two computer centres in Embilipitiya in December 2017. The computers required at both centres were provided by MBSL, investing Rs. 0.29 Mn thereby providing an opportunity for communities in the area to access technology.

Kegalle Vesak Project

MBSL sponsored the Kegalle Vesak Kalapaya in May 2017 at a total investment of Rs. 1.57 Mn. In addition to Vesak lanterns, banners and posters the Project featured the servicing of the Kegalle Nidahas Mawatha.

Natural Capital



As a responsible corporate citizen, we strive to minimise the environmental impact of our operations by reducing our energy, water and paper consumption. As a financial services provider, we are also cognisant of our ability in propagating environmentally-friendly business practices by ensuring that our borrowers are conscious of the potential negative environmental impacts of their businesses and processes.

Highlights of 2017

| | 2017 | 2016 | y-o-y % |
|-------------------------------|-----------|-----------|---------|
| Paper consumption | 394,924 | 291,761 | 35 |
| Energy consumption [Units] | 1,369,892 | 1,269,818 | 8 |
| Fuel consumption [Liters] | 44,300 | 28,441 | 56 |
| Carbon footprint [Kg] | 109,445 | 69,878 | 57 |

Strategy for 2017

- Implementation of core banking system is anticipated to result in substantial paper savings
- Ongoing focus on energy and water efficiencies

Environmental Management and Compliance

We consume natural resources in the form of energy, water and paper while our outputs comprise of waste and emissions. The Company's Environmental Management Framework ensures that all relevant environmental indicators are tracked on a consistent basis enabling us to identify areas for further improvement. Responsibility for ensuring compliance to all environmental regulations lies with the compliance division and monthly compliance reports are provided to the Board of Directors through the internal audit committee. During the year, there were no incidences of non-compliance to environmental regulations. We adopt precautionary principle when making investments decisions and environmental and local community impacts are given due consideration when balancing risk and growth opportunities.

Responsible Lending Practices

Engaging in green lending practices is a key short-to-medium term priority for the Company and we see strong potential in the hybrid and electric vehicles segment. The Company has also encouraged the

use of hybrid and electric vehicles through special leasing products, with the objective of reducing carbon emissions and reliance on fossil fuels.

Raw Materials

The Company's primary raw material is paper (used ISO 9001:2008, ISO 14001:2004, certified high quality "Double A Paper") which is consumed in its daily operations. We adopt a 3R approach of Reduce, Reuse and Re-cycle in order to minimise the use of paper. Process automation has also encouraged the reduction of paper usage; for example, the introduction of an automated employee attendance system allows employees to conduct administrative functions such as applying for leave digitally. Annual reports are also provided in hard copies only in the event of specific requests. We also actively discourage the use of unnecessary printing and photocopying.

The implementation of the Core Banking system is anticipated to result in a significant decline in the Company's paper consumption, facilitated by digital platforms for communication as well as self-service propositions for customers. In 2017 the Company's total paper consumption increased by 35% to 394,924 units. Details regarding the Company's material consumptions are given below;

| | 2017 | 2016 | 2015 |
|-------------------|---------|---------|---------|
| Paper consumption | 394,924 | 291,761 | 349,887 |
| Files | 15,064 | 15,568 | 12,601 |
| Toners | 290 | 407 | 389 |
| Ribbons | 450 | 430 | 370 |
| Other | 3,033 | 7,794 | 6,377 |

Energy

MBSL's electricity requirements are sourced in entirety from the national grid. Energy consumption is tracked at head office and all branches to effectively capture the Company's

Natural Capital

energy footprint and identify areas for improvement. Total electricity consumption for the year amounted to Rs. 1.37 million units, which reflected an increase of just 8% compared to the previous year. The Company's electricity and fuel consumption is given below.

| | 2017 | 2016 | 2015 |
|--------------------------------------|-----------|-----------|-----------|
| Electricity consumption (Units) | 1,369,892 | 1,269,818 | 1,138,679 |
| Petrol (Liters) | 25,410 | 11,158 | 10,983 |
| Diesel (Liters) | 18,889 | 17,281 | 14,617 |
| Electricity consumption per employee | 1,415 | 1,385 | 1,315 |
| Fuel consumption per employee | 46 | 31 | 24 |

Key initiatives for driving energy efficiency include increasing employee awareness through ongoing communications, use of energy efficient lighting solutions, use of double lighting panels and virtualising the server among others.

Water

The Company's operations are not water intensive, and water is only used for consumption by employees. Employees are engaged in water consumption through displays, posters and periodic notices. During the year, the Company's total water consumption efficiency decreased substantially by 13% to 15,350 units reflecting our ongoing efforts to enhance water efficiency. Water consumption per employee also declined by 16%. The Company's relies primarily on municipality lines for its water requirements with one branch obtaining water through ground sources. Consumption during the year is given below.

| | 2017 | 2016 | 2015 |
|--|--------|--------|--------|
| Total water consumption (Units) | 15,350 | 17,616 | 18,153 |
| Water consumption per employee (Units) | 16 | 19 | 21 |

Carbon footprint

The Company measures the carbon footprint of its the fuel consumed by its vehicles.

| Scope | | 2017 | 2016 | y-o-y % |
|-----------------|--|--------|--------|---------|
| Diesel (Liters) | | 18,889 | 17,281 | 9 |
| Petrol (Liters) | | 25,410 | 11,158 | 128 |



Robust governance
platform

Board of Directors



DR. S LOKUHEWA

Chairman [Non Executive Non Independent]

Dr. Sujeewa Lokuheva is currently the Chairman/Managing Director of Dhanaroso Holdings [Pvt] Ltd. and Universal Consultancy Services [Pvt] Ltd. positions he has held since 2009. He has extensive experience in the management of diverse businesses including real estate development, solar power products, Italian coffee shops and consultancy services. He also counts over twenty years' experience in reputed finance institutions at senior and middle level management positions and over ten years' experience at Board level in the areas of information technology, real estate, jewellery trade, pharmaceuticals, solar power, air-conditioning plants and hospitality businesses. He was also the Group Director/CEO of the EAP Regent Group for a period of five years.

In 2011, Dr. Lokuheva was the recipient of the UDC Master Class award for the best property development company presented by the former Prime Minister of Malaysia Dr. Mahathir Mohamed for the Company in which he was employed as Managing Director/CEO. During his career in the middle management he was also awarded the Best Senior Branch Manager for five consecutive years. Dr. Lokuheva was appointed as Chairman of MBSL Insurance Company Limited [MBSLI] in November 2016. Dr. Lokuheva holds an Honorary Doctorate in Philosophy [Ph.D.] in Business Administration awarded by the Open International University of Greece.



MR. S N DAYARATNE

Senior Director [Non Executive/Independent]

Mr. S. N. Dayaratne, Attorney-at-Law was admitted to the Bar in 1979 and counts over thirty eight years' experience as an active legal practitioner in labour, monetary and civil matters in Original Courts and Appellate courts. He graduated from the Law Faculty, University of Colombo in 1977. He has served as Chairman of Rent Board Kegalle for a period of six years and acted as the Company Secretary in three public bus companies namely Mawanella, Kegalle and Rambukkana until they were amalgamated as Sabaragamuwa Bus Company. He is presently serving as the Company Secretary of Hotel Athgiri [Pvt.] Ltd. and A M Aberathne & Sons [Pvt.] Ltd.



MR. D M GUNASEKERA

Non-Executive Non Independent Director

Mr. D. M. Gunasekera was nominated by the Bank of Ceylon to the Board of Merchant Bank of Sri Lanka & Finance PLC (MBSL) in February 2013 and was reappointed to the incumbent Board of MBSL with effect from 26th July 2016.

Mr. Gunasekera is a career banker with 34 years of diversified banking experience in corporate and offshore banking, sales and channel management and international banking operations. Prior to his appointment as Chief Executive Officer, he held a number of key corporate management positions in these areas. He possesses extensive experience in credit management and administration.

He holds a Special Degree in Public Finance and Taxation from the University of Colombo and has successfully completed the Program on Corporate Management (LKCM2) conducted by The Association for Overseas Technical Scholarship (AOTS) Japan and the Advanced Management Program on Corporate Management (AMP63) conducted by Wharton University of Pennsylvania, USA. He is also an Associate Member of the Institute of Bankers of Sri Lanka.

He has served as a Non-Executive Nominee Director on the Boards of several subsidiaries and associate companies of Bank of Ceylon including Bank of Ceylon (UK) Ltd., BoC Management & Support Service (Pvt.) Ltd., Ceybank Holiday Homes (Pvt.) Ltd., for the year 2016/2017. He served as a member on the Governing Board of the Institute of Bankers

of Sri Lanka (IBSL) and a member of the Association of Professional Bankers (APB Sri Lanka). He served as the Vice Chairman of Asia-Pacific Rural and Agricultural Credit Association (APRACA) for the year 2016/2017.

He was awarded the '100 GLOBAL SUSTAINABLE LEADERS (CEO) AWARD' in 2016 by the World Sustainability Congress in Dubai in recognition of most eminent professional and organizations as superlative Sustainability Leaders.

After an illustrious career at the Bank of Ceylon Mr. D. M. Gunasekera retired as the General Manager/Chief Executive Officer with effect from 22nd February 2018, consequent to which he tendered his resignation from MBSL with effect from 27th April 2018.

Board of Directors



MR. K B S BANDARA

Non-Executive/Non Independent Director

Mr. Bandara is attached to Bank of Ceylon and presently holds the position of General Manager. Prior to that, he has gained wide experience serving in several key areas of banking including Sales & Channel Management, International Banking Operations, Treasury Management, Corporate Lending, Development Banking and Electronic Banking in senior capacities. He also served as the Chief Executive Officer of Bank of Ceylon (UK) Ltd, London during 2011-2012.

Prior to joining the Bank, he served as an Assistant Lecturer at the University of Kelaniya, Sri Lanka and served at Mahaweli Authority. He had been a resource person at the Institute of Bankers of Sri Lanka in the field of credit and investment management too. He currently serves in the Governing Board of Institute of Bankers of Sri Lanka and is a director of BOC Travels (Pvt) Ltd, BOC Property Development & Management (Pvt) Ltd, Credit Information Bureau of Sri Lanka Ltd, Ceybank Asset Management Ltd, Hotels Colombo (1963) Ltd, Koladeniya Hydropower (Pvt) Ltd, Lanka Financial Services Bureau Ltd, Lanka Clear (Pvt) Ltd and Bank of Ceylon (UK) Ltd. He is the Chairman of BOC Management & Support Services (Pvt) Ltd and Ceybank Holiday Homes (Pvt) Ltd.

Mr. Bandara is a Physical Science graduate of the University of Kelaniya and holds a MBA with Merit Pass from the Postgraduate Institute of Management, University of Sri Jayewardenepura. Also, he has successfully completed Advanced Management Program conducted by the Harvard Business School, USA. He is a Fellow member of Institute of Bankers of Sri Lanka and obtained a Postgraduate Diploma in Bank Management from the same institute together with the best student award in 1998.



MR. W P R P H FONSEKA

Non-Executive Non-Independent Director

Mr. Fonseka, currently the Chief Financial Officer/Deputy General Manager (Corporate & Offshore Banking) of Bank of Ceylon (BOC) was nominated to the Board of Merchant Bank of Sri Lanka & Finance PLC (MBSL) on 26th July 2016 and was appointed as the Chairman of Audit Committee of MBSL with effect from 10th August 2016.

Mr. Fonseka is a professional banker along with over 27 years of extensive experience in both local and international commercial banking operations, specializing in financial management, strategic planning, corporate planning and budgetary control systems of BOC. He has been holding key corporate management positions in the areas of financial management, retail banking, international, treasury and investments of the Bank.

He serves as a Director on the Boards of Transnational Lanka Records Solutions (Private) Limited since November 2012, Lanka Securities (Private) Limited from April 2016, Property Development PLC and as an Alternate Director on the Boards of LankaClear (Private) Limited. Mr. Fonseka acts as the Chairman to the Audit Committees of Property Development PLC and LankaClear (Private) Limited as well.

Mr. Fonseka holds a Special Degree in Business Administration from the University of Sri Jayewardenepura, Sri Lanka, a Postgraduate Diploma in Management from the Postgraduate Institute of Management, Sri Lanka and a Master's Degree in Business Administration from the University of Southern Queensland, Australia. He is a Fellow Member of the Institute of Chartered Accountants of Sri Lanka and an Associate Member of the Institute of Bankers of Sri Lanka.



MR. N PERERA

Non Executive Independent Director

Mr. Niroshana Perera, Attorney-at-Law is a senior criminal lawyer, starting his legal career in the chambers of former President of the Bar Association of Sri Lanka Mr. Ananda Wijesekera P.C. He travels extensively appearing mainly in Magistrates' Courts and High Courts across the island. Mr. Perera has appeared in Intellectual Property, Bribery and corruption, debt recovery, defamation, labour related matters and other criminal cases of cheating, robbery, rape and murder. He has also been successfully retained by organisations as their Counsel with regard to cases filed under the Consumer Protection Authority and the Food Act.

A member of the Medico Legal Society of Sri Lanka, he is a highly respected member of the Bar Association for the past 20 years and was a Committee member of the Colombo Law Society for a period of five years. Mr. Niroshana Perera is presently the Chairman of the Industrial Technology Institute (former CISIR) of Sri Lanka. Whilst being the legal consultant of the Taekwondo Federation of Sri Lanka, he was one of the 3 Sri Lankan representatives at the Conservative Party Campaign in the United Kingdom in 2006.



MR. S P ARSAKULARATNE

Non Executive Independent Director

Mr. Arsakularatne, is a Partner of K.D.P. Arsakularatne & Sons, dealer Ceylon Petroleum Corporation. He was also the Deputy Chairman of Seethawakapura Urban Council. Mr. Arsakularatne counts several years' banking experience in the areas of credit administration, international trade, foreign currency and operations.

Corporate Management

As at 31 December 2017



1



2



5



6



7



10



11



12

1. Mr. N Karunapala - Chief Executive Officer
2. Mr. D Daluwatta - Chief Operating Officer
3. Ms. S Amaratunga - Senior Deputy General Manager
4. Mr. L Kaluarachchi - Deputy General Manager
5. Mr. J Gamalath - Deputy General Manager
6. Mrs. K Jayatilake - Deputy General Manager
7. Mr. S Uduwawala - Deputy General Manager
8. Mr. L Peiris - Deputy General Manager
9. Mr. K Jayasundara - Assistant General Manager
10. Mr. S Fernando - Assistant General Manager



- 11. Mr. C Withanachchi - Assistant General Manager
- 12. Mr. D Gunawardhana - Assistant General Manager
- 13. Mr. P Kandanaarachchi - Head of Finance
- 14. Mr. C Fernando - Head of Deposits

Corporate Management

As at 31 December 2017

Mr. N. Karunapala

Chief Executive Officer

Mr Nishaman Karunapala possesses over 25 years of experience with core expertise in finance leasing, trade and project finance, factoring, credit, recoveries, corporate strategy, system and process development and enterprise risk management. Prior to joining MBSL as CEO in July 2017, Mr Karunapala held the position of Director / Chief Executive Officer of Melsta Regal Finance Ltd, [MRFL] a former subsidiary of Melstacorp PLC. As the founding Director/CEO, he played a pivotal role at MRFL for over five years, since its inception in 2012.

Mr Karunapala was also instrumental in founding Orient Finance PLC, where he served a period of nine years since its inception in 2003 holding the positions of Assistant General Manager [Operations] and Deputy General Manager. He commenced his career at A. Baur and Co. Ltd. and moved to the financial services industry, initially at MBSL in 1992 and subsequently serving at Seylan Merchant Bank and Mercantile Leasing Ltd. His international exposure covers reputed financial institutions in Ireland, UK, Singapore, India and Philippines where he studied operational systems and procedures. He has also represented Sri Lanka in international training programs in Ireland, UK, Japan and Philippines.

He holds an MBA, Banking and Finance from the Postgraduate Institute of Management [PIM], BSc Business Administration [Special] Degree from the University of Sri Jayewardenepura and a Postgraduate Level Diploma in Modern Commercial Banking from PIM. He is also a member of the Certified Management Accountants [Australia]. Mr Karunapala is the Vice Chairman of the Financial

Houses Association [FHA] and a Committee member of Non-Banking Financial Sector Sub Committee - Chamber of Commerce. He is the immediate past chairman of the Leasing Association of Sri Lanka [LASL], having served two terms during 2011 – 2012 and 2014 to 2016. He was a Committee Member of the Ceylon Chamber of Commerce and a former Director of the Credit Information Bureau of Sri Lanka. Mr Karunapala is also a non executive director of MBSL Insurance Company [Pvt] Ltd.

Mr. D. Daluwatte

Chief Operating Officer

An experienced Banking and Finance professional, he counts over 29 years of Corporate Management experience in investment banking and corporate finance. He previously held the position of Deputy General Manager- Corporate Finance at Hatton National Bank and was the group Joint Managing Director of George Stewart & Company Ltd. Prior to his appointment as Chief Operating Officer of the Company he held the position of Chief Executive Officer at MCSL Financial Services [Pvt] Ltd. He is a fellow member of the Institute of Chartered Accountants of Sri Lanka, fellow member of the Chartered Institute of Management Accountants UK and member of the Chartered Institute for IT, UK. He has served as the Vice President of the Finance Houses Association of Sri Lanka [FHA] for a period of three years and has represented the FHA in the Committee of Ceylon Chamber of Commerce.

Ms. S. Amaratunga

Senior Deputy General Manager

Ms. Amaratunga has close to 27 years' experience and served as Head of several divisions of the Company such as Treasury, Trade Finance, Strategic Planning & Risk Management and Compliance Divisions. She also has extensive experience in Credit Management, Recoveries, Balance

Scorecard Performance Management System, Mergers & Acquisition processes, Restructuring, Finance and Cost Accounting and Human Resource. Currently, she is supervising Credit Administration, Risk Management and Compliance Divisions and Strategic Planning process of the Company. Ms. Amaratunga holds a MBA from the Postgraduate Institute of Management [University of Sri Jayewardenepura] and a Postgraduate Diploma Level Certificate for Modern Banking from PIM. She also holds a B.Com [Special] Degree from University of Jayewardenepura.

Mr. L. Kaluarachchi

He holds over 33 years' experience in the financial sector, bringing with him a diverse array of skills in credit, leasing and credit risk management. Making his entry into Merchant Banking in 1994, as the Manager Leasing, he subsequently progressed to hold the positions of DGM - Leasing, Acting CEO, DGM- Recoveries, DGM -Support Services, DGM - Range III and presently holding the position of DGM - Collection & Receivable Management. He holds a B,Com [Special] Degree from the University of Kelaniya.

Mr. J. Gamalath

Deputy General Manager - Marketing, Product Development & Region 2

He is a skilled marketing professional, with experience in multiple roles in sales and distribution, channel management, product and brand management and marketing communication. He has previously held senior marketing positions in leading telecommunication sector companies. Mr. Gamalath holds a Master of Business Studies from the University of Colombo and a Professional Postgraduate Diploma in Marketing from the Chartered Institute of Marketing UK.

Mrs. K. Jayatilake

Deputy General Manager - Legal/ Company Secretary

Mrs. Jayatilake is an Attorney-at-Law of the Supreme Court of Sri Lanka and a Notary Public counting over 26 years' experience at the Bar. She holds a Masters' Degree in Law [Commercial Law] from the University of Southampton [United Kingdom], a Bachelors' Degree in Arts with Second Class Honours [upper division pass] from the University of Colombo, in English, Economics and Political Science. Mrs. Jayatilake has worked in both the public and private sector as an in-house legal advisor at Senior Management level in addition to functioning as a Company Secretary. She has also worked as a Short Term Consultant with the World Bank.

Mr. S. Uduwawala

Deputy General Manager - Range 02 / Region 04

Mr. Uduwawala counts over 36 years of experience in the Banking industry, particularly in Credit and Branch Operations. He has extensive experience in three leading Commercial Banks in Sri Lanka and has worked for Nepal Sri Lanka Merchant Bank Ltd on secondment as its Manager- Credit on an overseas appointment. At present he is the Deputy General Manager - Range 02 / Region 04. Prior to taking over as DGM - Range 02 he was the Deputy General Manager of the Leasing Division, Branch Operations and also the Micro Finance Division.

Mr. L. Peiris

Deputy General Manager- Gold Loan & Support Services

Mr. Peiris counts over 33 years' experience in the banking sector, which include positions in Corporate Management, Senior Managerial and Managerial capacities in

diverse areas of exposure. His experience includes 6 years in the International Banking [Trade Finance] Division of Saudi British Bank, Riyadh, Saudi Arabia [HSBC Group] and 26 years in Sri Lanka including stints at Emirates Bank International Colombo Branch, Hatton National Bank, Seylan Bank, Ceylinco Savings Bank, MBSL Savings Bank and Merchant Bank of Sri Lanka & Finance PLC. His competency and skills are spread over International Trade, Banking Operations, Branch Banking and Administration, Business Development and Service Excellence. He holds a Bachelor of Arts in International Banking, Finance and Administration from the Trinity College and University- Spain.

Mr. K. Jayasundara

Assistant General Manager - Recoveries

Mr. Jayasundara has multi-faceted exposure in diverse areas in financial services and has previously held senior management positions in operations and credit. He holds a MBA in Banking & Finance offered from the Post Graduate Institute of Management (PIM) and a BSc [Hons] degree with a specialization in Agricultural Economics from University of Peradeniya. He also holds a Diploma in Credit Management from the Institute of Credit Management of Sri Lanka and is an Associate of the same Institute.

Mr. S. Fernando

Assistant General Manager - Internal Audit

Mr. Fernando is a member of the Institute of Internal Auditors [U.S.A] and is a Certified Internal Auditor [U.S.A]. He counts over 18 years of experience in the field of Internal Auditing in local conglomerates, as well as multinational companies.

Mr. C. Withanachchi

Assistant General Manager - Information Technology

Mr. Withanachchi counts over 18 years of diverse experience in Information Technology, including Software Developments, Design, System Administration and Delivery Management and exposure to Banking & Finance, ATM Implementation, Telecommunication and Manufacturing. He holds a BSc Degree in Information Technology and is currently reading for MSc in Information Security. He is also certified from IBM Corporation as an iSeries Expert on ILE RPG Programming and from the Indian Institute of Management - Bangalore for Innovation and IT Management.

Mr. D. Gunawardhana

Assistant General Manager - Human Resources

Mr. Dhammika Gunawardhana has extensive experience in HR Management in a variety of industry sectors. He is a fellow member of the Institute of Chartered Business Administrators, Professional member of Association of HR Professionals and a member of Institute of Personnel Management [IPM] and Institute of Management of Sri Lanka. He is also an Associate member of Institute of Certified Professional Managers, Sri Lanka Institute of Training & Development and National Institute of Professional Counselors.

Mr. Gunawardhana holds a BSc Degree in Business Administration from the University of Sri Jayewardenapura, BMS. Sp. Degree [Second Class Upper Honors] [Specialized in Human Resource Management] from the Open University of Sri Lanka. He holds a Diploma in Management from the Open University of Sri Lanka, Diplomas in Psychological counseling from the Institute of

Corporate Management

As at 31 December 2017

Psychological Studies & Department of Psychiatry, Faculty of Medical Sciences, University of Sri Jayawardhanapura and Diploma in Computer Science.

Under the Leadership of Mr. Gunawardhana, MBSL won both National and Asian Brand Awards on Best Service Provider in the year 2016 & 2017 respectively whilst winning the Global HR Excellence Award under the same category conferred by the World HRD Congress in 2018. He was also recognised among the "100 top global HR minds" at the same ceremony.

Mr. P. Kandanaarachchi

Head of Finance

Mr. Kandanaarachchi serves as the Head of Finance. He counts over 18 years' of experience in the fields of finance, auditing and accounting. He is an Associate member of The Institute of the Chartered Accountants of Sri Lanka.

Mr. Kandanaarachchi also serves as a Non-Executive Director on the Boards of MBSL Insurance Company Limited, subsidiary of the Company and Mega Containers Limited.

Mr. C. Fernando

Head of Deposits/ Region 01

A professional marketer with over 18 years' experience in Banking and Finance sector, handling Sales, Branch Operations, Investments, Treasury, Gold Loans, Marketing and Brand management, Credit Cards, Real Estate and Bancassurance.

Prior to joining MBSL he was attached to Softlogic Finance PLC, Standard Chartered Bank, Nations Trust Bank and HSBC.

Chamilantha holds a Bachelor's Degree from The University of Western Sydney, Australia majoring in Finance and Marketing and a Professional Postgraduate Diploma in Marketing (DipM) from the Chartered Institute of Marketing, UK. He is also a Member of Chartered Institute of Marketing, UK (MCIM)

He is a Practicing Marketer and a Member of Sri Lanka Institute of marketing (MSLIM) and an Associate Member of Institute of Bankers of Sri Lanka (AIB - SL)

Regional Managers

As at 31 December 2017



1. Mr. Sanjaya Ranatunga - Region 01
2. Mr. Ruwan Piyadasa - Region 02
3. Mr. Ratnasiri Mayakaduwa - Region 03
4. Mr. Keerthi Ramanayake - Region 04
5. Mr. S.P Niroshan - Region 05
6. Mr. Saman Pathmadeera - Region 06

Corporate Governance

MBSL is committed to maintaining high standards of integrity, transparency and ethical conduct, facilitated by robust governance practices. These standards are articulated through a suite of policies, the Director's Code of Ethics and well-defined structures which ensure the equitable treatment of all employees and judicious empowerment.

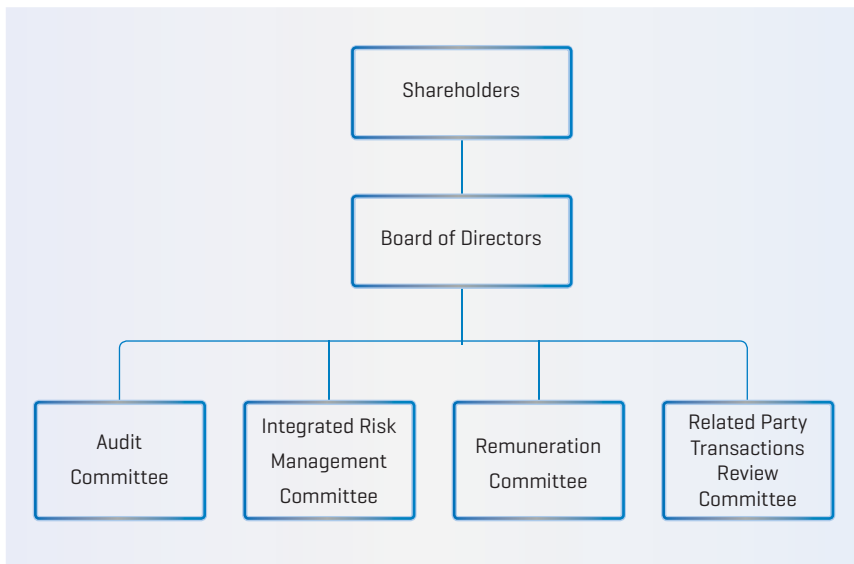
Governance Framework

MBSL's Corporate Governance framework has been developed to comply with the requirements of the Central Bank of Sri Lanka, the Colombo Stock Exchange and other relevant laws and regulations. In addition, the Company has voluntarily adopted the GRI Standards for Sustainability Reporting issued by the Global Reporting Initiative and the Integrated Reporting Framework issued by the International Integrated Reporting Council (IIRC). In terms of subsection [1][1] of Section 36 of the 19th Amendment (Amendment to Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka), the Auditor of the Company shall be the Auditor General of Sri Lanka.

| Standards and principles | | Governance systems |
|---|---|---|
| Internal | External | |
| <ul style="list-style-type: none"> Vision, Mission and Values Articles of Association Director's Code of Ethics Group's Corporate Governance Framework and practices Terms of References for Board and Board sub-committees Comprehensive framework of policies, systems and procedures | <ul style="list-style-type: none"> Companies Act No. 7 of 2007 Finance Companies [Corporate Governance] Direction No. 3 of 2008 Finance Leasing [Corporate Governance] Direction No. 4 of 2009 Listing Rules of the Colombo Stock Exchange Sri Lanka Accounting Standards Integrated Reporting Framework issued by the International Integrating Reporting Council (IIRC) GRI Standards for Sustainability reporting issued by the Global Reporting Initiative | <ul style="list-style-type: none"> Stakeholder engagement Strategic planning Risk management Compliance People management Internal and external audit Related Party Transactions |

The Board of Directors

The Board of Directors is the apex governing body and consisted of 7 Non-Executive Directors (including the Chairman) and two alternate directors of whom 3 are deemed independent as at 31 December 2017. Directors combine a variety of perspectives and skills including professional, academic and entrepreneurial insights which enhance the depth and overall effectiveness of decisions. The Board's responsibilities include determining the Company's strategic direction, defining governance structures, setting the risk appetite and formulating policy frameworks. The Board is supported by several sub-committees which oversight responsibility for specific areas.



| Board Sub-Committee | Mandate |
|---|---|
| Audit Committee | <ul style="list-style-type: none"> Ensuring the integrity of the Company's financial statements Review the adequacy and effectiveness of the Company's internal controls Ensures the internal audit activities are carried out objectively and independently |
| Integrated Risk Management Committee | <ul style="list-style-type: none"> Development and implementation of an integrated risk management framework Ensure compliance with all relevant regulations and legislations Monitors the adequacy of the contingency plans |
| Remuneration Committee | <ul style="list-style-type: none"> Makes recommendations to the Board on the remuneration paid to Executive Directors (if any) and the Chief Executive Officer |
| Related Party Transactions Review Committee | <ul style="list-style-type: none"> Review in advance all proposed related party transactions other than those transactions explicitly exempted in the Code. Adopting and reviewing policies and procedures on related party transactions of the Company and overseeing existing policies and procedures. Determining whether Related Party Transactions that are to be entered into by the Company require the approval of the Board of Directors or Shareholders of the Company |

The Board is also supported by seven management committees; namely Asset and Liability Management Committee, Investment Committee, NPL Committee, IT Steering Committee, Credit Committee, HR Committee and Real Estate Committee.

Board Meetings

The Board meets at least on a monthly basis with special meetings convened if and when the need arises. Board papers are circulated well in advance, providing adequate time for preparation. The Corporate Management is responsible for ensuring that timely and high quality information is provided to the Board, in sufficient time ahead of every meeting. Directors also receive regular briefings designed to update their skills and knowledge and also have the opportunity to participate in relevant external training sessions, such as those organized by the Sri Lanka Institute of Directors. The Board conducts a critical evaluation of its activities on an annual basis facilitated by the Company Secretary.

Director Training

Directors are provided access to training programmes to ensure that they are kept abreast of changes in regulatory developments, the industry landscape and technological advancements among others. During the year, Directors attended one (01) training programme conducted by the Ministry of Public Enterprise Development.

Corporate Governance

Guiding Strategy

The Board holds responsibility for formulating the Company's strategic agenda. Performance against the Strategic Plan is monitored based on a set of defined parameters covering earnings, financial position, credit quality and capitalisation among others. During the year, given challenges in the external and internal operating landscape, the Company revisited its strategy with the objectives of nurturing a performance driven culture, enhancing customer centricity and strengthening risk consciousness.

Risk Management and Internal Controls

The Board holds apex responsibility for maintaining sound risk management and internal control frameworks. It is also responsible for determining the risk appetite the Company is willing to take in achieving its growth aspirations. The risk management framework and risk performance during the year are described in the Risk Report on pages 105 to 114 and the Report of the Integrated Risk Management Committee on pages 103 & 104. Directors are also responsible for formulating and implementing a comprehensive framework of internal controls which ensure that assets are safeguarded and the integrity of financial reporting is preserved.

Section i

Compliance with Requirements on the Content of the Annual Report in Rule 7.6 of the Listing Rules

| CSE Rule No. | Governance Requirement | Extent of Compliance in 2017 |
|-------------------|--|---|
| 7.6 (i) | Names of persons who during the financial year were directors of the Company. | Please refer "Annual Report of the Board of Directors on the Affairs of the Company". |
| 7.6 (ii) | Principal activities of the Company and its Subsidiaries during the year and any changes therein. | Please refer "Annual Report of the Board of Directors on the Affairs of the Company". |
| 7.6 (iii) | The names and the number of shares held by the 20 largest holders of voting and non-voting shares and the percentage of such shares held. | Please refer "Financial Capital" for the 20 largest holders of voting shares. The Company has not issued any non-voting shares. |
| 7.6 (iv) | The public holding percentage. | Please refer "Financial Capital". |
| 7.6 (v) | Directors' and Chief Executive Officer's holding in shares of the Company at the beginning and end of the financial year. | Please refer "Financial Capital". |
| 7.6 (vi) | Information pertaining to material foreseeable risk factors. | Please refer "Risk Management Report". |
| 7.6 (vii) | Details of material issues pertaining to employees and industrial relations. | Please refer "Human Capital". |
| 7.6 (viii) | Extents, locations, valuations and the number of buildings of the land holdings and investment properties. | Please refer "Note 26" to the "Financial Statements". |
| 7.6 (ix) | Number of shares representing the stated capital. | Please refer "Note 38" to the "Financial Statements" on 'Capital'. |
| 7.6 (x) | A distribution schedule of the number of holders in each class of equity securities, and the percentage of their total holdings. | Please refer "Financial Capital". |
| 7.6 (xi) | Ratios and market price information on: EQUITY 1. Dividend per share. 2. Dividend payout. 3. Net asset value per share. 4. Market value per share [highest and lowest values recorded during the financial year and value as at the end of financial year]. DEBT 1. Interest rate of comparable government security. 2. Debt/equity ratio. 3. Interest cover. 4. Quick asset ratio. 5. The market prices & yield during the year. 6. Changes in credit rating. | Not applicable. Not applicable. Please refer "Statement of Financial Position". Please refer "Financial Capital". Please refer "Financial Capital". Please refer "Decade at a Glance". Please refer "Decade at a Glance". Please refer "Decade at a Glance". Please refer "Financial Capital". Please refer "Annual Report of the Board of Directors". |
| 7.6 (xii) | Significant changes in the Company's or its subsidiaries' fixed assets and the market value of land, if the value differs substantially from the book value. | Please refer "Note 27" to the "Financial Statements" on 'Property & Equipment'. |
| 7.6 (xiii) | Details of funds raised through a public issue, rights issue and a private placement. | The Company has not raised funds through a public issue, a rights issue or a private placement during the year 2017. |
| 7.6 (xiv) | Information in respect of Employee Share Option Schemes or Employee Share Purchase Schemes. | The Company does not have any Employee Share Option Schemes or Employee Share Purchase Schemes at present. |
| 7.6 (xv) | Disclosures pertaining to Corporate Governance practices in terms of rules 7.10.3, 7.10.5 c and 7.10.6 c of Section 7 of the Listing Rules. | This report provides the disclosures referred to in Rules 7.10.3, 7.10.5 c and 7.10.6 c of Section 7 of the Listing Rules. |
| 7.6 (xvi) | Related Party transactions exceeding 10% of the Equity or 5% of the total assets of the Entity as per Audited Financial Statements, whichever is lower. | The Company did not have any related party transactions exceeding this threshold during the year 2017. |

Corporate Governance

Section ii

Compliance with Listing Requirements on Corporate Governance Rules for Listed Companies issued by the Colombo Stock Exchange

| CSE Rule No. | Governance Requirement | Extent of Compliance in 2017 |
|---------------|---|---|
| 7.10.1 | Non-Executive Directors | |
| | a. The board shall include at least, two [2] non-executive directors; or such number of non-executive directors' equivalent to one third [1/3rd] of the total number of directors, whichever is higher. | Complied. All seven [07] directors who comprise the Board are non-executive directors, and have held office prior to and immediately preceding the Annual General Meeting. |
| | b. The total number of directors is to be calculated based on the number as at the conclusion of the immediately preceding Annual General Meeting. | |
| | c. Any change occurring to this ratio shall be rectified within ninety [90] days from the date of the change. | |
| 7.10.2 | Independent Directors | |
| | a. Where the constitution of the board includes only two [2] non-executive directors in terms of Rule 7.10.1 above, both such non-executive directors shall be "independent" (as per the criteria set out in Rule 7.10.4 of the CSE Listing Rules). In all other instances two [2] or one third [1/3rd] of non-executive directors appointed to the board, whichever is higher, shall be "independent". | Complied. Three [03] out of the seven [07] non executive directors are independent in terms of the criteria defined by CSE Rule 7.10.4. |
| | b. The board shall require each non-executive director to submit a signed and dated declaration annually of his/her independence or non-independence against the specified criteria. | Complied. |
| 7.10.3 | Disclosure relating to Directors | |
| | a. The board shall make a determination annually as to the independence or non-independence of each non-executive director based on such declaration and other information available to the board and shall set out in the Annual Report the names of directors determined to be "independent." | Complied. |
| | b. In the event a director does not qualify as "independent" against any of the criteria set out below but if the board, taking into account all the circumstances, is of the opinion that the director is nevertheless "independent" the board shall specify the criteria not met and the basis for its determination in the Annual Report. | Not applicable. |
| | c. In addition to disclosures relating to the independence of a director set out above, the board shall publish in its Annual Report a brief resume of each director on its board which includes information on the nature of his/her expertise in relevant functional areas. | Complied. Resume of each director is given on pages 52 to 55 of the Annual Report. |
| | d. Upon appointment of a new director to its board, the company shall forthwith provide to the Colombo Stock Exchange [the "Exchange"] a brief resume of such director for dissemination to the public. Such resume shall include information on the matters itemized in paragraphs [a], [b] and [c] above. | Complied. The Company Secretary has provided the required information to the Exchange upon appointment of new directors. |

| CSE Rule No. | Governance Requirement | Extent of Compliance in 2017 |
|---------------|--|---|
| 7.10.5 | Remuneration Committee | |
| | a. Composition | |
| | <p>The remuneration committee shall comprise; of a minimum of two [2] independent non-executive directors [in instances where the company has only two [2] directors on its board]; or of non-executive directors a majority of whom shall be independent, whichever is higher. One [1] non-executive director shall be appointed as Chairman of the committee by the board.</p> | <p>Complied. Remuneration Committee consists of five [05] non-executive directors, three [03] of whom are independent.</p> |
| | b. Functions | |
| | <p>The remuneration committee shall recommend the remuneration payable to the executive directors and Chief Executive Officer ["CEO"] of the company and/or equivalent position thereof, to the board of the company which will make the final determination upon consideration of such recommendations.</p> | <p>Complied. Please refer the "Remuneration Committee' Report on page 100 of the Annual Report.</p> |
| | c. Disclosure in the Annual Report | |
| | <p>The Annual Report should set out the names of directors [or persons in the parent company's committee in the case of a group company] comprising the remuneration committee, contain a statement of the remuneration policy and set out the aggregate remuneration paid to executive and non-executive directors.</p> | <p>Complied. The names of the members of the Remuneration Committee are given in the "Remuneration Committee Report" and the remuneration policy on page 100 of the Annual Report. Fees paid to directors are disclosed in the 'Notes to Financial Statements' on page 146 of the Annual Report.</p> |
| 7.10.6 | Audit Committee | |
| | a. Composition | |
| | <p>The audit committee shall comprise; of a minimum of two [2] independent non-executive directors [in instances where an entity has only two [2] directors on its board]; or of non-executive directors, a majority of whom shall be independent, whichever shall be higher. One [1] non-executive director shall be appointed as the Chairman of the audit committee by the board.</p> | <p>Complied.</p> |
| | <p>Unless otherwise determined by the audit committee, the CEO and the Chief Financial Officer ["CFO"] of the company shall attend audit committee meetings.</p> | <p>Complied.</p> |
| | <p>The Chairman or one [1] member of the audit committee should be a Member of a recognized professional accounting body.</p> | |

Corporate Governance

| CSE Rule No. | Governance Requirement | Extent of Compliance in 2017 |
|--------------|--|--|
| | <p>b. Functions</p> <p>The audit committee's functions shall include,</p> | |
| | (i) Overseeing of the preparation, presentation, and adequacy of disclosures in the financial statements of the company, in accordance with Sri Lanka Accounting Standards. | Complied. The functions of the audit committee and its Report are given on page 99. |
| | (ii) Overseeing of the company's compliance with financial reporting requirements, information requirements of the Companies Act No. 7 of 2007 and other relevant financial reporting related regulations and requirements. | Complied. |
| | (iii) Overseeing the processes to ensure that the company's internal controls and risk management are adequate to meet requirements of the Sri Lanka Auditing Standards. | Complied. |
| | (iv) Assessment of the independence and performance of the company's external auditors. | Not applicable. Since the Auditor General is the external auditor of the Bank where the independence is guaranteed under the Constitution of Sri Lanka and the Committee has no role to play in the engagement of the external auditor. |
| | (v) To make recommendations to the board pertaining to appointment, re-appointment and removal of the external auditors and to approve the remuneration and terms of engagement of the external auditors. | Not applicable. |
| | <p>c. Disclosure in the Annual Report</p> <p>The names of the directors (or persons in the parent company's committee in the case of a group company) comprising the audit committee should be disclosed in the Annual Report.</p> | Complied. The names of members of the audit committee and its report are given on page 98 of the Annual Report. |
| | <p>The audit committee shall make a determination of the independence of the auditors and shall disclose the basis for such determination in the Annual Report.</p> <p>The Annual Report shall contain a report by the audit committee setting out the manner of compliance by the company in relation to the above, during the period to which the Annual Report relates.</p> | Not applicable. The Auditor General is the auditor and his independence has been determined by the constitution |

Section iii

Compliance with Requirements on the Content of the Annual Report in Rule 7.6 of the Listing Rules

| Section | Governance Requirement | Extent of Compliance in 2017 |
|----------|--|--|
| 2 | The Responsibilities of the Board of Directors | |
| 2[1] | <p>The Board of Directors [hereinafter referred to as the Board] shall strengthen the safety and soundness of the finance company by-</p> <ul style="list-style-type: none"> a) Approving and overseeing the finance company’s strategic objectives and corporate values and ensuring that such objectives and values are communicated throughout the finance company; b) Approving the overall business strategy of the finance company, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least immediate next three [3] years; c) Identifying risks and ensuring implementation of appropriate systems to manage the risks prudently; d) Approving a policy of communication with all stakeholders, including depositors, creditors, shareholders and borrowers; e) Reviewing the adequacy and the integrity of the finance company’s internal control systems and management information systems; f) Identifying and designating key management personnel, who are in a position to: <ul style="list-style-type: none"> (i) Significantly influence policy; (ii) Direct activities; and (iii) Exercise control over business activities, operations and risk management; g) Defining the areas of authority and key responsibilities for the Board and for the key management personnel; h) Ensuring that there is appropriate oversight of the affairs of the finance company by key management personnel, that is consistent with the finance company’s policy; <ul style="list-style-type: none"> i) Periodically assessing the effectiveness of its own governance practices, including: <ul style="list-style-type: none"> (i) The selection, nomination and election of directors and appointment of key management personnel; (ii) The management of conflicts of interests; and (iii) The determination of weaknesses and implementation of changes where necessary; j) Ensuring that the finance company has an appropriate succession plan for key management personnel; k) Meeting regularly with the key management personnel to review policies, establish lines of communication and monitor progress towards corporate objectives; l) Understanding the regulatory environment; m) Exercising due diligence in the hiring and oversight of external auditors. | <p>Complied.</p> <p>The Strategic Plan for 2017- 2019 is available.</p> |
| 2[2] | The Board shall appoint the Chairman and the Chief Executive Officer (“CEO”) and define and approve the functions and responsibilities of the Chairman and the CEO in line with paragraph 7 of this Direction. | Complied. |
| 2[3] | There shall be a procedure determined by the Board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the finance company’s expense. The Board shall resolve to provide separate independent professional advice to directors to assist the relevant director[s] to discharge the duties to the finance company. | <p>Complied.</p> <p>Directors have obtained independent professional advice when necessary.</p> |
| 2[4] | A director shall abstain from voting on any Board resolution in relation to matter to which he or any of his relatives or a concern, in which he has substantial interest, is interested and he shall not be counted in the quorum for the relevant agenda item at the Board meeting. | <p>Not applicable.</p> <p>No such circumstance arose during the financial year under review.</p> |

Corporate Governance

| Section | Governance Requirement | Extent of Compliance in 2017 |
|----------|---|--|
| 2(5) | The Board shall have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the finance company is firmly under its authority. | Complied. |
| 2(6) | The Board shall, if it considers that the finance company is, or is likely to be, unable to meet its obligations or is about to become insolvent or is about to suspend payments due to depositors and other creditors, forthwith inform the Director of the Department of Supervision of Non-Bank Financial Institutions of the situation of the finance company prior to taking any decision or action. | Not applicable. No such circumstance arose during the financial year under review. |
| 2(7) | The Board shall include in the finance company's Annual Report, an annual corporate governance report setting out the compliance with this Direction. | Complied. The "Corporate Governance Report" is included in the Annual Report in pages 62 to 91. |
| 2(8) | The Board shall adopt a scheme of self-assessment to be undertaken by each director annually, and maintain records of such assessments. | Complied. |
| 3 | Meetings of the Board | |
| 3(1) | The Board shall meet at least twelve (12) times a financial year at approximately monthly intervals. Obtaining the Board's consent through the circulation of written or electronic resolutions/papers shall be avoided as far as possible. | Please refer page 91 of the Annual Report for details of attendance. |
| 3(2) | The Board shall ensure that arrangements are in place to enable all directors to include matters and proposals in the agenda for regular Board meetings where such matters and proposals relate to the promotion of business and the management of risks of the finance company. | Complied. |
| 3(3) | A notice of at least seven (7) days shall be given of a regular Board meeting to provide all directors an opportunity to attend. For other Board meetings, reasonable notice shall be given. | Complied. |
| 3(4) | A director who has not attended at least two-thirds (2/3rd) of the meetings in the period of twelve (12) months immediately preceding or has not attended the immediately preceding three (3) consecutive meetings held, shall cease to be a director. Provided, that participation at the directors' meetings through an alternate director shall, however, be acceptable as attendance. | Complied. |
| 3(5) | The Board shall appoint a Company Secretary whose primary responsibilities shall be to handle the secretarial services to the Board and shareholder meetings and to carry out other functions specified in the statutes and other regulations. | Complied. |
| 3(6) | If the Chairman has delegated to the Company Secretary the function of preparing the agenda for a Board meeting, the Company Secretary shall be responsible for carrying out such function. | Complied. |
| 3(7) | All directors shall have access to advice and services of the Company Secretary with a view to ensuring that Board procedures and all applicable laws, directions, rules and regulations are followed. | Complied. |
| 3(8) | The Company Secretary shall maintain the minutes of Board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any director. | Complied. |

| Section | Governance Requirement | Extent of Compliance in 2017 |
|----------|---|--|
| 3(9) | Minutes of Board meetings shall be recorded in sufficient detail so that it is possible to gather from the minutes, as to whether the Board acted with due care and prudence in performing its duties. The minutes of Board meeting shall clearly contain or refer to the following: (a) a summary of data and information used by the Board in its deliberations; (b) the matters considered by the Board; (c) the fact finding discussions and the issues of contention or dissent which may illustrate whether the Board was carrying out its duties with due care and prudence; (d) the explanations and confirmations of relevant executives which indicate compliance with the Board's strategies and policies and adherence to relevant laws and regulations; (e) the Board's knowledge and understanding of the risks to which the finance company is exposed and an overview of the risk management measures adopted; and (f) the decisions and Board resolutions. | Complied. |
| 4 | Composition of the Board | |
| 4(1) | The number of directors on the Board shall not be less than five (5) and not more than thirteen (13). | Complied. The Board including the Chairman comprises of seven (07) non – executive directors. |
| 4(2) | Subject to the transitional provisions contained herein and subject to paragraph 5(1) of this Direction the total period of service of a director other than a director who holds position of CEO or executive director shall not exceed nine (09) years. The total period in office of a non executive director shall be inclusive of the total period of service served by such director up to the date of this Direction. | Complied. |
| 4(3) | An employee of a finance company may be appointed, elected or nominated as a director of the finance company [hereinafter referred to as an "executive director"] provided that the number of executive directors shall not exceed one-half (1/2) of the number of directors of the Board. In such an event, one of the executive directors shall be the CEO of the company. | Not applicable. The Company has not appointed any executive directors. |
| 4(4) | The number of independent non-executive directors of the Board [as per the criteria for determining independence set out in this Direction] shall be at least one fourth (1/4th) of the total number of directors. | Complied. Please refer pages 95 to 96 of the Annual Report. |
| 4(5) | In the event an alternate director is appointed to represent an independent non-executive director, the person so appointed shall also meet the criteria that apply to the independent non-executive director. | Complied. Two (02) alternate directors have been appointed for two non independent non executive directors. |
| 4(6) | Non-executive directors shall have necessary skills and experience to bring an objective judgment to bear on issues of strategy, performance and resources. | Complied. Directors qualifications and experience are given in pages 52 to 55 of the Annual Report. |
| 4(7) | A meeting of the Board shall not be duly constituted, although the number of directors required to constitute the quorum at such meeting is present, unless at least one half (1/2) of the number of directors that constitute the quorum at such meeting are non-executive directors. | Complied. Please refer page 91 of the Annual Report. |
| 4(8) | The independent non-executive directors shall be expressly identified as such in all corporate communications that disclose the names of directors of the finance company. The finance company shall disclose the composition of the Board, by category of directors, including the names of the Chairman, executive directors, non-executive directors and independent non-executive directors in the annual corporate governance report which shall be an integral part of its Annual Report. | Complied. Please refer page 95 of the Annual Report. |

Corporate Governance

| Section | Governance Requirement | Extent of Compliance in 2017 |
|-----------|--|--|
| 4(9) | There shall be a formal, considered and transparent procedure for the appointment of new directors to the Board. There shall also be procedures in place for the orderly succession of appointments to the Board. | Complied. |
| 4(10) | All directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment. | Complied. |
| 4 (11) | If a director resigns or is removed from office, the Board shall announce to the shareholders and notify the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka, regarding the resignation of the director or removal and the reasons for such resignation or removal, including but not limited to information relating to the relevant director's disagreement with the Board, if any. | Complied. |
| 5 | Criteria to assess the fitness and propriety of directors | |
| 5(1) | A person over the age of seventy (70) years shall not serve as a director of the finance company. | Complied. |
| 5(2) | A director of the finance company shall not hold office as a director or any other equivalent position in more than twenty (20) companies/societies/ bodies corporate, including associate companies and subsidiaries of the finance company. Provided that such director shall not hold office of a director or any other equivalent position in more than ten (10) companies that are classified as Specified Business Entities in terms of the Sri Lanka Accounting and Auditing Standards Act, No. 15 of 1995. | Complied. |
| 6. | Delegation of Functions | |
| 6(1) | The Board shall not delegate any matters to a Board committee, CEO, executive directors or key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the Board as a whole to discharge its functions. | Complied. |
| 6(2) | The Board shall review the delegation of processes in place on a periodic basis to ensure that they remain relevant to the needs of the finance company. | Complied. |
| 7 | The Chairman and the Chief Executive Officer | |
| 7(1) | The roles of the Chairman and the CEO shall be separate and shall not be performed by one and the same person. | Complied. |
| 7(2) | The Chairman shall be a non-executive director. In the case where the chairman is not an independent non-executive director, the Board shall designate an independent non-executive director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the finance company's Annual Report. | Complied. The company has appointed an independent non-executive director as the Senior Director . Please refer page 95 of the "Annual Report of the Board of Director's on the affairs of the Company". |
| 7(3) | The Board shall disclose in its corporate governance report, which shall be an integral part of its Annual Report, the name of the Chairman and the CEO and the nature of any relationship [including financial, business, family or other material /relevant relationship(s)], if any, between the Chairman and the CEO and the relationships among members of the Board. | Complied. |

| Section | Governance Requirement | Extent of Compliance in 2017 |
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| 7(4) | The Chairman shall : (a) Provide leadership to the Board; (b) Ensure that the Board works effectively and discharges its responsibilities; and (c) Ensure that all key issues are discussed by the Board in a timely manner. | Complied. |
| 7(5) | The Chairman shall be primarily responsible for the preparation of the agenda for each Board meeting. The Chairman may delegate the function of preparing the agenda to the Company Secretary. | Complied |
| 7(6) | The Chairman shall ensure that all directors are informed adequately and in a timely manner of the issues arising at each Board meeting. | Complied |
| 7(7) | The Chairman shall encourage each director to make full and active contribution to the Board's affairs and take the lead to ensure that the Board acts in the best interests of the finance company. | Complied |
| 7(8) | The Chairman shall facilitate the effective contribution of non-executive directors in particular and ensure constructive relationships between executive and non-executive directors. | Complied. There are no executive directors on the Board. |
| 7(9) | The Chairman shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever. | Complied |
| 7 (10) | The Chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of the shareholders are communicated to the Board. | Complied. The Annual General Meeting ("AGM"), Annual Report and Interim Financial Statements of the Company are the principal means of communication with shareholders. The Board invites the shareholders to raise their concerns on the affairs of the Company at the AGM as a means of maintaining an appropriate dialogue with them. The external auditors and lawyers are also present at the AGM to answer any queries raised by shareholders. |
| 7 (11) | The CEO shall function as the apex executive-in-charge of day-to-day management of the finance company's operations and business. | Complied. |
| 8 | Board appointed Committees | |
| 8(1) | Every finance company shall have at least the two [2] Board committees set out in paragraph 8(2) and 8(3) of these Directions. Each committee shall report directly to the Board. Each committee shall appoint a secretary to arrange its meetings, maintain minutes, records and carry out such other secretarial functions under the supervision of the chairman of the committee. The Board shall present a report on the performances, duties and functions of each Committee, at the annual general meeting of the finance company. | Complied. The Audit Committee, Remuneration Committee, Integrated Risk Management Committee and the Related Party Transactions Review Committee which are Board appointed sub committees, regularly report to the Board. Please refer pages 98,100,101 and 103 of the Annual Report. |

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| 8(2) | Audit Committee The following shall apply in relation to the Audit Committee: | |
| 8(2) (a) | The chairman of the audit committee shall be a non-executive director who possesses qualifications and experience in accountancy and/or audit. | Complied. |
| 8 (2) (b) | The Board members appointed to the audit committee shall be non-executive directors. | Complied. The Audit Committee consists of five (5) non- executive directors, three (3) of whom are independent. |
| 8 (2) (c) | The audit committee shall make recommendations on matters in connection with: <ul style="list-style-type: none"> (i) The appointment of the external auditor for audit services to be provided in compliance with the relevant statutes; (ii) The implementation of the Central Bank guidelines issued to external auditors from time to time, (iii) The application of the relevant accounting standards; and (iv) The service period, audit fee and any resignation or dismissal of the auditor, provided that the engagement of an audit partner shall not exceed five (5) years, and that the particular audit partner is not re-engaged for the audit before the expiry of three (3) years from the date of the completion of the previous term. | Not applicable. The Auditor General is the external auditor of MBSL. Complied. Complied. Not Applicable. Auditor General has been appointed in terms of subsection (1)(1) of Section 36 of the 19th amendment (amendment to the Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka. |
| 8 (2) (d) | The Audit Committee shall review and monitor the external auditor's independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices. | Not applicable. MBSL's auditor being the Auditor General, his independence and effectiveness is guaranteed under the Constitution of Sri Lanka. |
| 8 (2) (e) | The audit committee shall develop and implement a policy with the approval of the Board on the engagement of an external auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines. In doing so, the audit committee shall ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the audit committee shall consider: <ul style="list-style-type: none"> (i) Whether the skills and experience of the auditor make it a suitable provider of the non-audit services; (ii) Whether there are safeguards in place to ensure that there is no threat to the objectivity and/or independence in the conduct of the audit resulting from the provision of such services by the external auditor; and (iii) Whether the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the auditor, pose any threat to the objectivity and/or independence of the external auditor. | Not Applicable. This does not arise since the Auditor General is the Auditor of MBSL. |

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| 8 [2] [f] | The audit committee shall, before the audit commences, discuss and finalize with the external auditors, the nature and scope of the audit, including: [i] an assessment of the finance company's compliance with the Directions issued under the Finance Companies Act No. 78 of 1988 [the "Act"] and the management's internal controls over financial reporting; [ii] the preparation of financial statements in accordance with relevant accounting principles and reporting obligations; and [iii] the co-ordination between auditors where more than one [1] auditor is involved. | Complied. The scope and extent of audit have been determined by the Auditor General. |
| 8 [2] [g] | The audit committee shall review the financial information of the finance company, in order to monitor the integrity of the financial statements of the finance company, its annual report, accounts and periodical reports prepared for disclosure, and the significant financial reporting judgments contained therein. In reviewing the finance company's annual report and accounts and periodical reports before submission to the Board, the audit committee shall focus particularly on: [i] major judgmental areas; [ii] any changes in accounting policies and practices; [iii] significant adjustments arising from the audit; [iv] the going concern assumption; and [v] the compliance with relevant accounting standards and other legal requirements. | Complied. The Audit Committee reviews the Company's financial statements including the quarterly unaudited financial statements and the audited financial statements prior to recommending same to the Board for approval. |
| 8 [2] [h] | The audit committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary. | Complied. The Audit Committee discusses issues, problems and reservations arising from the final audit. The representatives of BDO Partners, Chartered Accountants, who assisted the Auditor General in the year 2017 audit, met the Audit Committee. |
| 8 [2] [i] | The audit committee shall review the external auditor's management letter and the management's response thereto. | Complied. |
| 8 [2] [j] | The audit committee shall take the following steps with regard to the internal audit function of the finance company: [i] Review the adequacy of the scope, functions and resources of the internal audit department, and satisfy itself that the department has the necessary authority to carry out its work; [ii] Review the internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the internal audit department; [iii] Review any appraisal or assessment of the performance of the head and senior staff members of the internal audit department; [iv] Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function; [v] Ensure that the audit committee is apprised of resignations of senior staff members of the internal audit department including the Chief Internal Auditor and any outsourced service providers, and to provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning; [vi] Ensure that the internal audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care. | Complied. |

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| 8 (2) [k] | The audit committee shall consider the major findings of internal investigations and management's responses thereto; | Complied. Significant findings of the internal audit are deliberated by the Audit Committee with the management and recommendations are referred to the Board. |
| 8 (2) [l] | The CFO, the chief internal auditor and a representative of the external auditors may normally attend meetings. Other Board members and the CEO may also attend meetings upon the invitation of the audit committee. However, at least once in six (6) months, the audit committee shall meet with the external auditors without the executive directors being present. | Complied Please refer the Audit Committee Report on pages 98 to 99 of the Annual Report for details. |
| 8 (2) [m] | The audit committee shall have: [i] explicit authority to investigate into any matter within its terms of reference; [ii] the resources which it needs to do so; [iii] full access to information; and [iv] authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary. | Complied. |
| 8 (2) [n] | The audit committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities. | Complied. |
| 8 (2) [o] | The Board shall, in the Annual Report, disclose in an informative way, [i] Details of the activities of the audit committee; [ii] The number of audit committee meetings held in the year; and [iii] Details of attendance of each individual member at such meetings. | Complied. Please refer pages 91 & 99 of the Annual Report for details of attendance of each individual member at audit committee meetings. |
| 8 (2) [p] | The secretary to the audit committee (who may be the company secretary or the head of the internal audit function) shall record and keep detailed minutes of the audit committee meetings. | Complied. The Head of Internal Audit acts as Secretary of the Audit Committee. |
| 8 (2) [q] | The audit committee shall review arrangements by which employees of the finance company may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the audit committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the finance company's relations with the external auditor. | Complied. The Company has introduced a "whistle blowing policy" to enable employees to report any irregularities of the Company. In the event of any improprieties being reported, the Internal Audit Department is authorized to carry out an immediate inquiry into the matter and report its observations to the chairman and the Audit Committee. |
| 8 (3) | Integrated Risk Management Committee The following shall apply in relation to the Integrated Risk Management Committee ["IRMC"]: a) The IRMC shall consist of at least one [1] non-executive director, CEO and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The IRMC shall work with key management personnel closely and make decisions on behalf of the Board within the framework of the authority and responsibility assigned to the IRMC. | Complied. Please refer the Report on "Risk Management" pages 105 to 114 of the Annual Report for details. |

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| | <p>b) The IRMC shall assess all risks, i.e. credit, market, liquidity, operational and strategic risks to the company on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on the company basis and group basis.</p> <p>c) The IRMC shall review the adequacy and effectiveness of all management level committees such as the credit committee and the asset – liability committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the IRMC.</p> <p>d) The IRMC shall take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the IRMC on the basis of the company's policies and regulatory and supervisory requirements.</p> <p>e) The IRMC shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans.</p> <p>f) The IRMC shall take appropriate actions against officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the IRMC, and/or as directed by the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central bank of Sri Lanka.</p> <p>g) The IRMC shall submit a risk assessment report within a week of each meeting to the Board, seeking the Board's views, concurrence and/or specific directions.</p> <p>h) The IRMC shall establish a compliance function to assess the company's compliance with laws, regulations, directions, rules, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the IRMC periodically.</p> | <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> |
| 9. | Related Party Transactions | |
| 9[2] | <p>The Board shall take necessary steps to avoid any conflicts of interest that may arise from any transaction of the finance company with any person, and particularly with the following categories of persons who shall be considered as "related parties" for the purposes of this Direction:</p> <p>a) A subsidiary of the finance company;</p> <p>b) Any associate company of the finance company;</p> <p>c) A director of the finance company;</p> <p>d) A key management personnel of the finance company;</p> <p>e) A relative of a director or a key management personnel of the finance company ;</p> <p>f) A shareholder who owns shares exceeding ten percent [10%] of the paid up capital of the finance company;</p> <p>g) A concern in which a director of the finance company or a relative of a director or a shareholder who owns shares exceeding ten percent [10%] of the paid up capital of the finance company, has substantial interest.</p> | <p>Complied.</p> <p>Transactions with related parties have been carried out in the ordinary course of business and on an arms-length basis.</p> |
| 9[3] | <p>The transactions with a related party that are covered in this Direction shall be the following:</p> <p>a) Granting accommodation,</p> <p>b) Creating liabilities to the finance company in the form of deposits, borrowings and investments,</p> <p>c) Providing financial or non-financial services to the finance company or obtaining those services from the finance company,</p> | |

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| | d) Creating or maintaining reporting lines and information flows between the finance company and any related party which may lead to share proprietary, confidential or otherwise sensitive information that may give benefits to such related party. | |
| 9(4) | <p>The Board shall ensure that the finance company does not engage in transactions with a related party in a manner that would grant such party "more favourable treatment" than that is accorded to other similar constituents of the finance company. For the purpose of this paragraph "more favourable treatment" shall mean:</p> <p>a) Granting of "total net accommodation" to a related party, exceeding a prudent percentage of the finance company's regulatory capital, as determined by the Board. The "total net accommodation" shall be computed by deducting from the total accommodation, the cash collateral and investments made by such related party in the finance company's share capital and debt instruments with a remaining maturity of five (5) years or more.</p> <p>b) Charging a rate of interest lower than the finance company's best lending rate or paying a rate of interest exceeding the rate paid for a comparable transaction with an unrelated comparable counterparty.</p> <p>c) Providing preferential treatment, such as favorable terms, covering trade losses and/ or waiving fees/commissions, that extends beyond the terms granted in the normal course of business with unrelated parties;</p> <p>d) Providing or obtaining services to or from a related-party without a proper evaluation procedure;</p> <p>e) Maintaining reporting lines and information flows between the company and any related party which may lead to share proprietary, confidential or otherwise sensitive information that may give benefits to such related party, except as required for performance of legitimate duties and functions.</p> | <p>Complied.</p> <p>Please refer Note 41 under "Notes to the Financial Statements" on pages 196 to 198 of the Annual Report.</p> |
| 10 | Disclosures | |
| 10 [1] | The Board shall ensure that: (a) annual audited financial statements and periodical financial statements are prepared and published in accordance with the formats prescribed by the regulatory and supervisory authorities and applicable accounting standards, and that (b) such statements are published in the newspapers in an abridged form, in Sinhala, Tamil and English. | Complied. |
| 10 [2] | <p>The Board shall ensure that at least the following disclosures are made in the Annual Report:</p> <p>a) A statement to the effect that the annual audited financial statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures.</p> | <p>Complied.</p> <p>Please refer "Directors' Responsibility for Financial Reporting" on page 118 of the Annual Report.</p> |
| | b) A report by the Board on the finance company's internal control mechanism that confirms that the financial reporting system has been designed to provide a reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements has been done in accordance with relevant accounting principles and regulatory requirements. | <p>Complied.</p> <p>Please refer pages 116 & 117 of the Annual Report for the relevant report by the Board.</p> |
| | c) The external auditor's certification on the effectiveness of the internal control mechanism in respect of any statements prepared or published. | <p>Complied.</p> <p>Please refer page 117.</p> |
| | d) Details of directors, including names, transactions with the finance company. | <p>Complied.</p> <p>Please refer page 196 of the Annual Report for details.</p> |

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| | e) Fees/remuneration paid by the finance company to the directors in aggregate. | Complied. Please refer page 96 of the Annual Report for details. |
| | f) Total net accommodation as defined in paragraph 9(4) of this Direction outstanding in respect of each category of related parties and the net accommodation outstanding in respect of each category of related parties as a percentage of the finance company's capital funds. | Complied. Please refer Note 41 under "Notes to the Financial Statements" on pages 196 to 198 of the Annual Report. |
| | g) The aggregate values of remuneration paid by the finance company to its key management personnel and the aggregate values of the transactions of the finance company with its key management personnel during the financial year, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the finance company. | Complied. Please refer Note 41 under "Notes to the Financial Statements" on pages 196 to 198 of the Annual Report. |
| | h) A report setting out the details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any non-compliances. | Complied. Please refer the "Annual Report of the Board of Directors on the Affairs of the Company" and the Statement of "Directors' Responsibilities for Financial Reporting" on pages 96 and 118 respectively of the Annual Report for details. |
| | i) A statement of the regulatory and supervisory concerns on lapses in the finance company's risk management, or non compliance with the Act, and rules and directions that have been communicated by the Director of the Department of Supervision of Non-Bank Financial Institutions, if so directed by the Monetary Board to be disclosed to the public, together with the measures taken by the finance company to address such concerns. | Finance Companies [Corporate Governance] Direction No.03 of 2008 Section 2 [1] j Corrective actions have been taken for all matters |
| | j) The external auditor's certification of the compliance with the Act and rules and directions issued by the Monetary Board in the annual corporate governance reports. | The external auditors have adopted procedures set out in Sri Lanka Standards on Related Service 4750 issued by the Institute of Chartered Accountants of Sri Lanka [SLSRS 4750], to meet the compliance requirements of the Corporate Governance Directions. Their findings presented in their report addressed to the board are consistent with the matters disclosed above and did not identify any material inconsistencies to those reported above by the Board. |

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Finance Leasing (Corporate Governance) Direction No.4 of 2009 for Registered Finance Leasing Establishments

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| 2 | The Responsibilities of the Board of Directors | |
| 2 [1] | <p>The Board is responsible for strengthening the safety and soundness of the company by-</p> <p>a) Approving and overseeing the company's strategic objectives and corporate values and ensuring that such objectives and values are communicated throughout the company;</p> <p>b) Approving the overall business strategy of the company, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least immediate next three (3) years;</p> <p>c) Identifying risks and ensuring implementation of appropriate systems to manage the risks prudently;</p> <p>d) Approving policy of communication with all stakeholders of the company, including lenders, creditors, shareholders and borrowers;</p> <p>e) Reviewing the adequacy and the integrity of the company's internal control systems and management information systems;</p> <p>f) Identifying and designating key management personnel who are in a position to (i) significantly influence policy ;(ii) direct activities; and (iii) exercise control over business activities, operations and risk management;</p> <p>g) Defining the areas of authority and key responsibilities for the Board and for the key management personnel;</p> <p>h) Ensuring that there is appropriate oversight of the affairs of the company by key management personnel, that is consistent with the company's policy;</p> <p>i) Periodically assessing the effectiveness of its own governance practices, including</p> <p>(i) The selection, nomination and election of directors and appointment of key management personnel;</p> <p>(ii) The management of conflicts of interests; and</p> <p>(iii) The identification of weaknesses and implementation of changes where necessary;</p> <p>j) Ensuring that the company has an appropriate succession plan for key management personnel;</p> <p>k) Meeting regularly with the key management personnel to review policies, establish lines of communication and monitor progress towards corporate objectives;</p> <p>l) Understanding the regulatory environment;</p> <p>m) Exercising due diligence in the hiring and oversight of external auditors;</p> | <p>Complied.</p> <p>The Strategic Plan for 2017 -2019 is available.</p> |
| 2[2] | The Board shall appoint the Chairman and Chief Executive Officer ("CEO") and define and approve their functions and responsibilities in line with paragraph 7 of this Direction. | Complied. |

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| 2 [3] | The Board shall determine a procedure to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the company's expense. The Board shall resolve to provide separate independent professional advice to directors to assist the relevant director(s) to discharge the duties to the company. | Complied. The directors have obtained independent professional advice when necessary. |
| 2 [4] | A director shall abstain from voting on any Board resolution in relation to a matter in which he or any of his relatives or a concern, in which he has substantial interest, is interested and he shall not be counted in the quorum for the relevant agenda item at the Board meeting. | Not applicable. No such circumstance arose during the financial year under review. |
| 2 [5] | The Board shall have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the company is firmly under its authority. | Complied. |
| 2 [6] | The Board shall, if it considers that the company is, or is likely to be, unable to meet its obligations or is about to become insolvent or is about to suspend payments due to lenders and other creditors, forthwith inform the Director of the Department of Supervision of Non-Bank Financial Institutions of the situation of the company prior to taking any decision or action. | Not applicable. No such circumstance arose during the financial year under review. |
| 2 [7] | The Board shall include in the company's Annual Report, an annual corporate governance report setting out the compliance with this Direction. | Complied. The "Corporate Governance Report" is included in the Annual Report in pages 62 to 91. |
| 2 [8] | The Board shall adopt a scheme of self – assessment to be undertaken by each director annually, and maintain records of such assessment. | Complied. |
| 3 | Meetings of the Board | |
| 3 [1] | The Board shall meet at least twelve [12] times a financial year at approximately monthly intervals. Obtaining the Board's consent through the circulation of written or electronic resolution/papers shall be avoided as far as possible. | Complied. Please refer page 91 of the Annual Report for details of attendance. |
| 3 [2] | The Board shall ensure that arrangements are in place to enable all directors to include matters and proposals in the agenda for regular Board meetings where such matters and proposals relate to the promotion of business and the management of risks of the company. | Complied. |
| 3 [3] | A notice of at least seven [7] days shall be given of a regular Board meeting to provide all directors an opportunity to attend. For other Board meetings, reasonable notice shall be given. | Complied. |
| 3 [4] | A director who has not attended at least two-thirds [2/3rd] of the meetings in the period of twelve [12] months immediately preceding or has not attended the immediately preceding three [3] consecutive meetings held, shall cease to be a director. Provided, that participation at the director's meetings through an alternate director shall, however, be acceptable as attendance. | Complied. |
| 3 [5] | The Board shall appoint a company secretary whose primary responsibilities shall be to handle the secretarial services to the Board and shareholder meetings and to carry out other functions specified in the statutes and other regulations. | Complied. |
| 3 [6] | If the chairman has delegated to the company secretary the function of preparing the agenda for a Board meeting, the company secretary shall be responsible for carrying out such function. | Complied. |

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| 3 [7] | All directors shall have access to advice and services of the company secretary with a view to ensuring that Board procedures and all applicable laws, directions, rules and regulations are followed. | Complied. |
| 3 [8] | The company secretary shall maintain the minutes of Board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any director. | Complied. |
| 3 [9] | Minutes of Board meetings shall be recorded in sufficient detail so that it is possible to gather from the minutes, as to whether the Board acted with due care and prudence in performing its duties. The minutes of a Board meeting shall clearly contain or refer to the following: [a] a summary of data and information used by the Board in its deliberations; [b] the matters considered by the Board; [c] the fact finding discussions and the issues of contention or dissent which may illustrate whether the Board was carrying out its duties with due care and prudence; [d] the explanations and confirmations of relevant executives which indicate compliance with the Board's strategies and policies and adherence to relevant laws and regulations; [e] the Board's knowledge and understanding of the risks to which the company is exposed and an overview of the risk management measures adopted; and [f] the decisions and Board resolutions. | Complied. |
| 4 | Composition of the Board | |
| 4 [1] | The number of directors on the Board shall not be less than five [5] and not more than nine [9]. | Complied. The Board including the Chairman comprises of seven [07] non-executive directors. |
| 4 [2] | Subject to paragraph 5[1] of this Direction and the transitional provisions contained herein the total period of service of a director other than a director who holds position of CEO or executive director shall not exceed nine [9] years. The total period in office of a non-executive director shall be inclusive of the total period of service served by such director up to the date of this Direction. | Complied. |
| 4 [3] | An employee of the company may be appointed, elected or nominated as a director of the company (hereinafter referred to as an "executive director") provided that the number of executive directors shall not exceed one-half [1/2] of the number of directors of the Board. In such an event, one of the executive directors shall be the CEO of the company. | Not applicable. The Company has not appointed any executive directors. |
| 4 [4] | The number of independent non-executive directors of the Board (as per the criteria for determining independence set out in this Direction) shall be at least one fourth [1/4th] of the total number of directors. | Complied. Please refer to pages 95 & 96 of the Annual Report. |
| 4 [5] | In the event an alternate director is appointed to represent an independent non-executive director, the person so appointed shall also meet the criteria that apply to the independent non-executive director. | Complied. Two [02] alternate directors have been appointed for two non independent non-executive directors . |
| 4 [6] | Non-executive directors shall have necessary skills and experience to bring an objective judgment to bear on issues of strategy, performance and resources. | Complied. Directors' qualifications and experience are given in pages 52 to 55 of the Annual Report. |

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| 4 [7] | A meeting of the Board shall not be duly constituted, although the number of directors required to constitute the quorum at such meeting is present, unless at least one third [1/3rd] of the number of directors that constitute the quorum at such meeting are non-executive directors. | Complied. Please refer page 91 of the Annual Report. |
| 4 [8] | The independent non-executive directors shall be expressly identified as such in all corporate communications that disclose the names of directors of the company. The company shall disclose the composition of the Board, by category of directors, including the names of the chairman, executive directors, non-executive directors and independent non-executive directors in the annual corporate governance report which shall be an integral part of its Annual Report. | Complied. Please refer page 95 of the Annual Report. |
| 4 [9] | There shall be a formal, considered and transparent procedure for the appointment of new directors to the Board. There shall also be procedures in place for the orderly succession of appointments to the Board. | Complied. |
| 4 [10] | All directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment. | Complied. |
| 4 [11] | If a director resigns or is removed from office, the Board shall announce to the shareholders and notify the Director of the Department of Supervision of Non-Bank Financial Institutions regarding the resignation of the director or removal and the reasons for such resignation or removal, including but not limited to information relating to the relevant director's disagreement with the Board, if any. | Complied. |
| 5 | Criteria to assess the fitness and propriety of directors | |
| 5 [1] | A person over the age of seventy [70] years shall not serve as a director of the company. | Complied. |
| 5 [2] | A director of the company shall not hold office as a director or any other equivalent position in more than twenty [20] companies/societies/ bodies corporate, including associate companies and subsidiaries of the company. Provided that such director shall not hold office of a director or any other equivalent position in more than ten [10] companies that are classified as Specified Business Entities in terms of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995. | Complied. |
| 6 | Management functions delegated to the Board | |
| 6 [1] | The Board shall not delegate any matters to a Board committee, CEO, executive directors or key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the Board as a whole to discharge its functions. | Complied. |
| 6 [2] | The Board shall review the delegation of processes in place on a periodic basis to ensure that they remain relevant to the needs of the company. | Complied. |
| 7 | The Chairman and the Chief Executive Officer | |
| 7 [1] | The roles of the Chairman and the CEO shall be separated and shall not be performed by one and the same person. | Complied. |

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| Section | Governance Requirement | Extent of Compliance in 2017 |
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| 7 [2] | The Chairman shall be a non-executive director. In the case where the Chairman is not an independent non-executive director, the Board shall designate an independent non-executive director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the company's Annual Report. | Complied. The company has appointed an independent non-executive director as the Senior Director. Please refer page 95 of the "Annual Report of the Board of Director's on the affairs of the Company". s |
| 7 [3] | The Board shall disclose in its corporate governance report, which shall be an integral part of its Annual Report, the name of the Chairman and the CEO and the nature of any relationship [including financial, business, family or other material /relevant relationship(s)], if any, between the chairman and the CEO and the relationships among members of the Board. | Complied. |
| 7 [4] | The Chairman shall : (a) Provide leadership to the Board; (b) Ensure that the Board works effectively and discharges its responsibilities; and (c) Ensure that all key issues are discussed by the Board in a timely manner. | Complied. |
| 7 [5] | The Chairman shall be primarily responsible for the preparation of the agenda for each Board meeting. The Chairman may delegate the function of preparing the agenda to the company secretary. | Complied. |
| 7 [6] | The Chairman shall ensure that all directors are informed adequately and in a timely manner of the issues arising at each Board meeting. | Complied. |
| 7 [7] | The Chairman shall encourage each director to make full and active contribution to the Board's affairs and take the lead to ensure that the Board acts in the best interests of the company. | Complied. |
| 7 [8] | The Chairman shall facilitate the effective contribution of non-executive directors in particular and ensure constructive relationships between executive and non-executive directors. | Complied. There are no executive directors on the Board. |
| 7 [9] | The Chairman shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever. | Complied. |
| 7 [10] | The Chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of the shareholders are communicated to the Board. | Complied. The Annual General Meeting ["AGM"], Annual Report and Interim Financial Statements of the Company are the principal means of communication with shareholders. The Board invites the shareholders to raise their concerns on the affairs of the Company at the AGM as a means of maintaining an appropriate dialogue with them. The external auditors and lawyers are also present at the AGM to answer any queries raised by shareholders. |
| 7 [11] | The CEO shall function as the apex executive-in-charge of day-to-day management of the company's operations and business. | Complied. |

| Section | Governance Requirement | Extent of Compliance in 2017 |
|-----------|---|---|
| 8 | Board appointed Committees | |
| 8 [1] | Every company shall have at least two [2] Board committees set out in paragraph 8[2] and 8[3] of this Direction. Each committee shall report directly to the Board. Each committee shall appoint a secretary to arrange its meetings, maintain minutes, records and carry out such other secretarial functions under the supervision of the chairman of the Committee. The Board shall present a report on the performances, duties and functions of each Committee, at the AGM of the Company. | Complied. The Audit Committee, Remuneration Committee, Integrated Risk Management Committee and the Related Party Transactions Review Committee which are Board appointed sub committees, regularly report to the Board. Please refer pages 98,100,101 & 103 of the Annual Report. |
| 8 [2] | Audit Committee The following shall apply in relation to the Audit Committee: | |
| 8 [2] [a] | The chairman of the audit committee shall be a non-executive director who possesses qualifications and experience in accountancy and/or audit. | Complied. |
| 8 [2] [b] | The majority of the Board members appointed to the audit committee shall be non-executive directors. | Complied. |
| 8 [2] [c] | The audit committee shall make recommendations on matters in connection with: (i) The appointment of the external auditor for audit services to be provided in compliance with the relevant statutes; (ii) The implementation of the Central Bank guidelines issued to external auditors from time to time, (iii) The application of the relevant accounting standards; and (iv) The service period, audit fee and any resignation or dismissal of the external auditor, provided that the engagement of an audit partner shall not exceed five [5] years, and that the particular audit partner is not re-engaged for the audit before the expiry of three [3] years from the date of the completion of the previous term. | Not applicable. The Auditor General is the external auditor of MBSL. Complied. Complied. Not applicable. The Auditor General is the external auditor of MBSL. |
| 8 [2] [d] | The audit committee shall review and monitor the external auditor's independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices. | Not Applicable. MBSL's auditor being the Auditor General his independence and effectiveness is guaranteed under the Constitution of Sri Lanka. |

Corporate Governance

| Section | Governance Requirement | Extent of Compliance in 2017 |
|-----------|---|--|
| 8 [2] (e) | <p>The audit committees shall develop and implement a policy with the approval of the Board on the engagement of an external auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines. In doing so, the audit committee shall ensure that provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditors independence or objectivity in relation to the provision of non-audit services, the audit committee shall consider:</p> <p>(i) Whether the skills and experience of the auditor make it a suitable provider of the non-audit services;</p> <p>(ii) Whether there are safeguards in place to ensure that there is no threat to the objectivity and/or independence in the conduct of the audit resulting from the provision of such services by the external auditor; and</p> <p>(iii) Whether the nature of the non-audit services, the related fee levels individually and in aggregate relative to the auditor, pose any threat to the objectivity and/or independence of the external auditor.</p> | <p>Not Applicable.</p> <p>This does not arise since the Auditor General is the Auditor of MBSL.</p> |
| 8 [2] (f) | <p>The audit committee shall, before the audit commences, discuss and finalize with the external auditors, the nature and scope of the audit, including: (i) an assessment of the company's compliance with Directions issued under the Finance Leasing Act No. 56 of 2000 and the management's internal controls over financial reporting; (ii) the preparation of financial statements in accordance with relevant accounting principles and reporting obligations; and (iii) the co-ordination between auditors where more than one [1] auditor is involved.</p> | <p>Complied.</p> <p>The scope and extent of audit have been determined by the Auditor General.</p> |
| 8 [2] (g) | <p>The audit committee shall review the financial information of the company, in order to monitor the integrity of the financial statements of the company, its Annual Report, accounts and periodical reports prepared for disclosure, and the significant financial reporting judgments contained therein. In reviewing the company's Annual Report and accounts and periodical reports before submission to the Board, the Audit Committee shall focus particularly on: (i) major judgmental areas; (ii) any changes in accounting policies and practices; (iii) significant adjustments arising from the audit; (iv) the going concern assumption; and (v) the compliance with relevant accounting standards and other legal requirements.</p> | <p>Complied.</p> <p>The Audit Committee reviews the Company's financial statements including the quarterly unaudited financial statements and the audited financial statements prior to recommending same to the Board for approval.</p> |
| 8 [2] (h) | <p>The audit committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary.</p> | <p>Complied.</p> <p>The Audit Committee discusses issues, problems and reservations arising from the final audit. The representatives of BDO Partners, Chartered Accountants, who assisted the Auditor General in the year 2017 audit met the Audit Committee.</p> |
| 8 [2] (i) | <p>The audit committee shall review the external auditor's management letter and the management's response thereto.</p> | <p>Complied.</p> <p>2017 Management Letter discussion is in progress</p> |

| Section | Governance Requirement | Extent of Compliance in 2017 |
|-----------|--|---|
| 8 [2] [j] | <p>The audit committee shall take the following steps with regard to the internal audit function of the company:</p> <ul style="list-style-type: none"> (i) Review the adequacy of the scope, functions and resources of the internal audit department, and satisfy itself that the department has the necessary authority to carry out its work; (ii) Review the internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the internal audit department; (iii) Review any appraisal or assessment of the performance of the head and senior staff members of the internal audit department; (iv) Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function; (v) Ensure that the audit committee is apprised of resignations of senior staff members of the internal audit department including the Chief Internal Auditor and any outsourced service providers, and to provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning; (vi) Ensure that the internal audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care; | Complied. |
| 8 [2] [k] | The audit committee shall consider the major findings of internal investigations and management's responses thereto; | Complied. Significant findings of the internal audit are deliberated by the Audit Committee with the management and recommendations are referred to the Board. |
| 8 [2] [l] | The CFO, the Chief Internal Auditor and a representative of the external auditors may normally attend audit committee meetings. Other Board members and the CEO may also attend meetings upon the invitation of the Audit Committee. However, at least once in six [6] months, the audit committee shall meet with the external auditors without the executive directors of the Company being present. | Complied. Please refer the Audit Committee Report on pages 98 & 99 of the Annual Report for details. |
| 8 [2] [m] | The audit committee shall have: (i) explicit authority to investigate into any matter within its terms of reference; (ii) the resources which it needs to do so; (iii) full access to information; and (iv) authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary. | Complied. |
| 8 [2] [n] | The audit committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities. | Complied. |
| 8 [2] [o] | <p>The Board shall, in the Annual Report, disclose in an informative way,</p> <ul style="list-style-type: none"> (i) Details of the activities of the audit committee; (ii) The number of audit committee meetings held in the year; and (iii) Details of attendance of each individual member at such meetings. | Complied. Please refer pages 91 & 99 of the Annual Report for details of attendance of each individual member at Audit Committee meetings. |

Corporate Governance

| Section | Governance Requirement | Extent of Compliance in 2017 |
|-----------|---|--|
| 8 [2] [p] | The secretary to the audit committee (who may be the company secretary or the head of the internal audit function) shall record and keep detailed minutes of the Audit Committee meetings. | Complied. The Head of Internal Audit acts as Secretary of the Audit Committee. |
| 8 [2] [q] | The audit committee shall review arrangements by which employees of the finance company may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the audit committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the finance company's relations with the external auditor. | Complied. The Company has introduced a "whistle blowing policy" to enable employees to report any irregularities of the Company. In the event of any improprieties being reported, the Internal Audit Division is authorized to carry out an immediate inquiry into the matter and report its observations to the chairman and the Audit Committee. |
| 8 [3] | <p>Integrated Risk Management Committee</p> <p>The following shall apply in relation to the Integrated Risk Management Committee ("IRMC"):</p> <p>a) The IRMC shall consist of at least one [1] non-executive director, CEO and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The IRMC shall work with key management personnel closely and make decisions on behalf of the Board within the framework of the authority and responsibility assigned to the IRMC.</p> <p>b) The IRMC shall assess all risks, i.e, credit, market, liquidity, operational and strategic risks to the company on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on the company basis and group basis.</p> <p>c) The IRMC shall review the adequacy and effectiveness of all management level committees such as the credit committee and the asset –liability committee to address specific risks and to manage those risks within quantitative risk limits as specified by the IRMC.</p> <p>d) The IRMC shall take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the IRMC on the basis of the company's policies and regulatory and supervisory requirements.</p> <p>e) The IRMC shall meet, at least quarterly, to assess all aspects of risk management including updated business continuity plans.</p> <p>f) The IRMC shall take appropriate actions against officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the IRMC, and/or as directed by the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka.</p> | <p>Complied.</p> <p>Please refer the Report of the Risk Management on pages 105 to 114 of the Annual Report for details.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> <p>Complied.</p> |
| | g) The IRMC shall submit a risk assessment report within a week of each meeting to the Board, seeking the Board's views, concurrence and/or specific directions. | Complied. |
| | h) The IRMC shall establish a compliance function to assess the company's compliance with laws, regulations, directions, rules, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the IRMC periodically. | Complied. |

| Section | Governance Requirement | Extent of Compliance in 2017 |
|-----------|--|---|
| 9. | Related Party Transactions | |
| 9 [2] | <p>The Board shall take necessary steps to avoid any conflicts of interest that may arise from any transaction of the company with any person, and particularly with the following categories of persons who shall be considered as "related parties" for the purposes of this Direction:</p> <ul style="list-style-type: none"> a) A subsidiary of the company; b) Any associate company of the company; c) A director of the company; d) A key management personnel of the company; e) A relative of a director or a key management personnel of the company ; f) A shareholder who owns shares exceeding ten percent (10%) of the paid up capital of the company; g) A concern in which a director of the company or a relative of a director or a shareholder who owns shares exceeding ten percent (10%) of the paid up capital of the company, has substantial interest. | <p>Complied.</p> <p>Transactions with related parties have been carried out in the ordinary course of business and on an arms length basis.</p> |
| 9 [3] | <p>The transactions with a related party that are covered in this Direction shall be the following:</p> <ul style="list-style-type: none"> (a) Granting accommodation, (b) Creating liabilities to the company in the form of borrowings or investments, (c) Providing financial or non-financial services to the company or obtaining those services from the company, (d) Creating or maintaining reporting lines and information flows between the company and any related party which may lead to share proprietary, confidential or otherwise sensitive information that may give benefits to such related party. | Complied |
| 9 [4] | <p>The Board shall ensure that the company does not engage in transactions with a related party in a manner that would grant such party "more favorable treatment" than that is accorded to an unrelated comparable counterparty of the company. For the purpose of this paragraph "more favorable treatment" shall mean:</p> <ul style="list-style-type: none"> a) Granting of "total net accommodation" to a related party, exceeding a prudent percentage of the company's regulatory capital, as determined by the Board. The "total net accommodation" shall be computed by deducting from the total accommodation, the cash collateral and investments made by such related party in the company's share capital and debt instrument with a remaining maturity of five (5) years. b) Charging a rate of interest lower than the company's best lending rate or paying a rate of interest exceeding the rate paid for a comparable transaction with an unrelated comparable counterparty. c) Providing preferential treatment, such as favorable terms, covering trade losses and/ or waiving fees/commissions, that extends beyond the terms granted in the normal course of business with unrelated parties; d) Providing or obtaining services to or from a related-party without a proper evaluation procedure; e) Maintaining reporting lines and information flows between the company and any related party which may lead to share proprietary, confidential or otherwise sensitive information that may give benefits to such related party, except as required for performance of legitimate duties and functions. | <p>Complied.</p> <p>Please refer Financial Statements, Note 41 - "Related party Transactions" on pages 196 to 198 of the Annual Report.</p> |

Corporate Governance

| Section | Governance Requirement | Extent of Compliance in 2017 |
|------------|---|--|
| 10. | Disclosures | |
| 10 [1] | The Board shall ensure that annual audited financial statements and periodical financial statements are prepared and published in accordance with the requirements of the regulatory and supervisory authorities and applicable accounting standards. | Complied. |
| 10 [2] | The Board shall ensure that at least the following disclosures are made in the Annual Report: | Complied. |
| 10 [2] (a) | A statement to the effect that the annual audited financial statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures. | Please refer "Directors' Responsibility for Financial Reporting" on page 118 of the Annual Report. |
| 10 [2] (b) | A report by the Board on the company's internal control mechanism that confirms that the financial reporting system has been designed to provide a reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements has been done in accordance with relevant accounting principles and regulatory requirements. | Complied. Please refer pages 116 & 117 of the Annual Report for the relevant report by the Board. |
| 10 [2] (c) | The external auditor's certification on the effectiveness of the internal control mechanism in respect of any statements prepared or published. | Complied. Please refer page 117. |
| 10 [2] (d) | Details of directors, including names, transactions with the company. | Complied. Please refer page 196 of the Annual report for details. |
| 10 [2] (e) | Fees/remuneration paid by the company to the directors in aggregate. | Complied. Please refer page 96 of the Annual Report for details. |
| 10 [2] (f) | Total net accommodation as defined in paragraph 9(4) of this Direction outstanding in respect of each category of related parties and the net accommodation outstanding in respect of each category of related parties as a percentage of capital funds of the company. | Complied. Please refer 'Note 41' under "Notes to the Financial Statements" on pages 196 to 198 of the Annual Report. |
| 10 [2] (g) | The aggregate values of remuneration paid by the company to its key management personnel and the aggregate values of the transactions of the company with its key management personnel during the financial year, set out by broad categories such as remuneration paid, accommodation granted and borrowing through debt instruments or investments made in the company. | Complied. Please refer 'Note 41' under "Notes to the Financial Statements" on pages 196 & 197 of the Annual Report. |
| 10 [2] (h) | A report setting out the details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any non-compliance. | Complied. Please refer the "Annual Report of the Board of Directors" on the Affairs of the Company and the Statement of "Directors' Responsibilities for Financial Reporting" on pages 96 to 118 respectively of the Annual Report for details. |

| Section | Governance Requirement | Extent of Compliance in 2017 |
|------------|---|--|
| 10 [2] (i) | The external auditor's certification of the compliance with the Finance Leasing Act No. 56 of 2000 and directions issued by the Director of Department of Supervision of Non-Bank Financial Institutions in the annual corporate governance reports . | The external auditors have adopted procedures set out in Sri Lanka Standards on Related Service 4750 issued by the Institute of Chartered Accountants of Sri Lanka (SLSRS 4750), to meet the compliance requirements of the Corporate Governance Directions. Their findings presented in their report addressed to the board are consistent with the matters disclosed above and did not identify any material inconsistencies to those reported above by the Board. |

Attendance at the Meetings of the Board & Sub-Committees held during the financial year 2017

| Name of the Director | Directorship Status | Board | Audit Committee | Remuneration Committee | Integrated Risk Management Committee | Related Party Transactions Review Committee |
|--|---|----------------------|-----------------|------------------------|--------------------------------------|---|
| | | No. of Meetings Held | | | | |
| | | 25 | 12 | - | 06 | 02 |
| Dr. S. Lokuhewa | Non Independent Non Executive Director | 25 | N/A | - | N/A | N/A |
| Mr. C. N. Wijewardane [Resigned w.e.f. 10/08/2017] | Non Independent Non Executive Director | 14 | N/A | - | 04 | 01 |
| Mr. D. M. Gunasekara | Non Independent Non Executive Director | 23 | N/A | - | N/A | N/A |
| Mr. D.M.L.B. Dassanayake [Alt. Director to Mr. D.M.Gunasekara] | Non Independent Non Executive Director | 01 | N/A | - | N/A | N/A |
| Mr. W. P. R. P. H. Fonseka | Non Independent Non Executive Director | 22 | 11 | - | N/A | 02 |
| Mr. K. B. S. Bandara | Non Independent Non Executive Director | 16 | 04 | - | 05 | 00 |
| Mr.R.M.D.V. Jayabahu [Alt. Director to Mr. K. B. S. Bandara] | Non Independent Non Executive Director | 04 | 04 | - | 00 | 02 |
| Mr. N. Perera | Independent Non Executive Director | 24 | 12 | - | 01 | N/A |
| Mr. S. N. Dayaratne | Senior Independent Non Executive Director | 24 | 11 | - | 01 | 02 |
| Mr. S. P. Arsakularatne | Independent Non Executive Director | 24 | 10 | - | N/A | 02 |
| Mr. H. J. D. Fonseka [Resigned w.e.f. 28/09/2017] | Independent Non Executive Director | 14 | 10 | - | 04 | 01 |

Annual Report of the Board of Directors on the Affairs of the Company

GENERAL

The Directors have the pleasure in presenting to the shareholders their Report together with the Audited Financial Statements for the year ended 31 December 2017 of Merchant Bank of Sri Lanka & Finance PLC.

Merchant Bank of Sri Lanka & Finance PLC is a public limited liability company incorporated on 04 March 1982 under the Companies Ordinance [Cap.145], re-registered under the provisions of the Companies Act No.07 of 2007 and is quoted on the Colombo Stock Exchange since 1991. The Company is registered as a Finance Company licensed under the

Finance Business Act No. 42 of 2011 and registered as a Finance Leasing Company under the Finance Leasing Act No. 56 of 2000.

The Audited Financial Statements included in this Annual Report have been prepared and presented with the relevant disclosures in accordance with the Sri Lanka Accounting Standards and other applicable regulatory requirements.

The Registered Office of the Company is situated at Bank of Ceylon Merchant Tower, No. 28, St. Michael's Road, Colombo 03 at which the Company's head office is also located.

This Report provides the information as required by the Companies Act No. 07 of 2007, the Listing Rules of the Colombo Stock Exchange and the recommended best practices on Corporate Governance. This Report was approved by the Board of Directors on 17 May 2018.

Section 168 of the Companies Act No. 07 of 2007, requires the following information to be published in the Annual Report and is disclosed hereunder in respect of the year under review [i.e., for the year ended 31 December 2017]

| Information required to be disclosed as per the Companies Act No. 07 of 2007 | Reference [section of the Companies Act No. 7 of 2007] | Extent of compliance by the Company |
|--|--|-------------------------------------|
| i The nature of the business of the Group and the Company together with any change thereof during the accounting period and the classes of business in which the Company has an interest. | Section 168 [1] [a] | Refer on page 128 |
| ii Signed Financial Statements of the Company and the Group for the accounting period completed | Section 168 [1] [b] | Refer on page 125 |
| iii Auditors' Report on the Financial Statements of the Company and of the Group | Section 168 [1] [c] | Refer on page 119 |
| iv Accounting Policies and any changes therein [Group also included] | Section 168 [1] [d] | Refer on page 128 |
| v Particulars of the entries made in the Interest Register during the accounting period | Section 168 [1] [e] | Refer on page 196-197 |
| vi Director's fee and other benefits paid to Directors of the Company and its subsidiaries during the accounting period | Section 168 [1] [f] | Refer on page 96 |
| vii Information on donations made by the Company during the accounting period | Section 168 [1] [g] | Refer on page 96 |
| viii Names of Directors of the Company as at the end of the accounting period and the names of persons who ceased to hold office as directors during the accounting period | Section 168 [1] [h] | Refer on page 95 |
| ix Disclosure on amounts payable to the Auditor as Audit Fees and a separate disclosure on amounts payable to the Auditor as Fees for other services rendered during the accounting period | Section 168 [1] [i] | Refer on page 96 |
| x Particulars of the Auditors' relationship with the Company and/ or any of its subsidiaries [other than that of Auditor] or any interest the Auditor has in the Company and/or its Subsidiaries | Section 168 [1] [j] | Refer on page 96 |
| xi Acknowledgement of the contents of this Report/Signatures on behalf of the Board by any two directors and the Company Secretary | Section 168 [1] [k] | Refer on page 97 |

Vision, Mission and Corporate Conduct

The Company's vision, mission and values are given on page 01 of this Report.

Principal Activities

The Company is a registered Finance Leasing Company under the provisions of the Finance Leasing Act No.56 of 2000 and a Finance Company licensed by the Monetary Board of Central Bank of Sri Lanka under the Finance Business Act No 42 of 2011. The Company is also a registered Market Intermediary by the Securities and Exchange Commission of Sri Lanka under the categories of (i) Margin Provider (ii) Underwriter and (iii) Investment Manager. MBSL has a subsidiary and an associate Company namely, MBSL Insurance Company Limited and Lanka Securities (Private) Limited respectively, which collectively constitute the Group.

The principal activities of the Company are Leasing and Hire Purchase, Corporate and Retail Credit, Corporate Advisory, Capital Market activities, Lending to SMEs and Agriculture sectors, Deposit mobilization and the Provision of other related financial services.

The principal activities of the subsidiary and associate are given in Note 1.3 to the Financial Statements on page 128.

Review of Operations

A review of the operations of the Company during the financial year ended 31 December 2017 and results of those operations are contained in the Chairman's Review on pages 8 to 9 and Management Discussion and Analysis on pages 25 to 30. These reports form an integral part of the Annual Report.

Future Outlook

An overview of the future plans and developments of the Company is presented in the Chairman's review on pages 8 to 9 of this Annual Report.

Financial Statements of the Company and the Group

The Audited Financial Statements of the Company and of the Group for the year ended 31 December 2017 duly signed by the Head of Finance, the Chief Executive Officer and approved by the Board of Directors of the Company are given on pages 124 to 227 and form an integral part of this Report of the Board.

Directors' Responsibility for Financial Reporting

The Board of Directors are responsible for the preparation of the Financial Statements of the Group and the Company, which reflects a true and fair view of the state of affairs of the Company and of the Group. The Directors are of the view that the Statement of Profit or Loss, Statement of Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows, Significant Accounting Policies and Notes thereto appearing on pages 122 to 227 have been prepared in conformity with the requirements of the Sri Lanka Accounting Standards as mandated by the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 and the Companies Act No. 07 of 2007. Further, these Financial Statements also comply with the requirements of the Finance Leasing Act No. 56 of 2000, Finance Business Act No 42 of 2011, Regulation of Insurance Industry

Act No 43 of 2000 and the Banking Act No 30 of 1988 and amendments thereto and the Listing Rules of the Colombo Stock Exchange. The 'Statement of Directors' Responsibility for Financial Reporting' appearing on page 118 forms an integral part of this Report.

Auditors' Report

The Auditor General is the Auditor of Merchant Bank of Sri Lanka & Finance PLC in terms of the provisions of Article 154(4) of the Constitution of the Democratic Socialist Republic of Sri Lanka. Report of the Auditor General on the Financial Statements of the Company and the Consolidated Financial Statements for the year ended 31 December 2017 is given on pages 119 to 120 of this Annual Report.

Significant Accounting Policies and Changes During the Year

During the year under review, there were no changes in the accounting policies that had been adopted by the Group and the Company were consistent with those adopted in the previous financial year as required by the Sri Lanka Accounting Standards- LKAS 01 on 'Presentation of Financial Statements' and comply with Section 168 (1) (d) of the Companies Act No. 07 of 2007. The Significant Accounting Policies adopted in the preparation of the Financial Statements of the Group and the Company are given on pages 128 to 227 of the Annual Report.

Income

The income of the Company for the year ended 31 December 2017 was Rs.6,403 Mn (2016-Rs. 4,888). An analysis of the Income is given in Note 4 to the Financial Statements on page 141.

Annual Report of the Board of Directors on the Affairs of the Company

Financial Results and Appropriations

Details of the Company and Group performance and appropriation of profit are tabulated as follows.

| For the year ended 31 December | Company | | Group | |
|---|----------|----------|----------|----------|
| | 2017 | 2016 | 2017 | 2016 |
| | Rs.Mn | Rs.Mn | Rs.Mn | Rs.Mn |
| Profit before taxation | 228.65 | 232.90 | 239.46 | 239.82 |
| Taxation | (127.80) | (154.25) | (136.11) | (165.66) |
| Profit after taxation | 100.85 | 78.65 | 103.35 | 74.16 |
| Non-controlling interest | - | - | 8.5 | 36.71 |
| Profit for the year/Profit attributable to the Parent Company | 100.85 | 78.65 | 111.85 | 110.87 |
| Profit brought forward from the previous year | 846.19 | 747.41 | 859.58 | 726.30 |
| Profit available for appropriation | 947.04 | 826.06 | 971.43 | 837.17 |
| Appropriations | | | | |
| Other comprehensive income | (1.92) | 37.25 | (2.85) | 39.53 |
| Transfer to reserves | (20.17) | (17.12) | (20.17) | (17.12) |
| Total appropriation | (22.09) | 20.13 | (23.02) | 22.41 |
| Un-appropriated profit carried forward | 924.95 | 846.19 | 948.41 | 859.58 |

Reserves

A summary of Company and Group reserves are given in below table.

| For the year ended 31 December | Company | | Group | |
|--------------------------------|---------|---------|--------|---------|
| | 2017 | 2016 | 2017 | 2016 |
| | Rs.Mn | Rs.Mn | Rs.Mn | Rs.Mn |
| Statutory Reserve Fund | 177.84 | 157.67 | 177.84 | 157.67 |
| Available for Sale Reserve | 6.58 | (21.80) | 1.30 | (36.20) |
| Retained Earnings | 924.95 | 846.19 | 948.41 | 859.58 |

Information on the movement of reserves are given in the Statement of Changes in Equity on page 126 and in Note 39 respectively to the Financial Statements on page 195.

Taxation

The Company is liable for income tax at the rate of 28% (2016-28%) and VAT on Financial Services at 15%.

Statutory Payments

The Board of Directors confirm that to the best of their knowledge and belief, statutory payments to all relevant regulatory and statutory authorities have been paid by the Company.

Property, Equipment and Intangible Assets

The total capital expenditure incurred on the acquisition of property, equipment and intangible assets of the Group and the Company amounted to Rs. 311.29 Mn and 311.13 Mn respectively. The details of property, equipment and intangible assets of the Company are given in Note 27 & 28 to the Financial Statements on pages 178 to 185.

Market Value of Freehold Properties

All freehold land and buildings of the Company were revalued by a professionally qualified independent valuer. The Directors are of the opinion that the carrying amount is not in excess of the current market values of the property. The details of freehold property owned by the Company are given in Note 27 to the Financial Statements on page 180.

Issue of Shares and Debentures

The Company did not issue any shares during the financial year. Company issued two billion Unsecured subordinated redeemable debentures with a par value of Rs. 100 each.

Stated Capital and Debentures

The Company's Stated Capital as at 31 December 2017 was Rs. 2,124.46 Mn., comprising of 165,874,541 ordinary voting shares. The details of the Stated Capital are given in Note 38 to the Financial Statements on page 194.

The details of debentures redeemed during the year ended 31 December 2017 and those outstanding as at 31 December 2017 are given in Note 32.1 to the Financial Statements on page 187.

Capital Adequacy

The Company ensures that it maintains the statutory requirement on core capital and supplementary capital, to mitigate the liquidity risk and safe guard the depositors, thus ensuring the sustainability of the

Company and the industry as a whole. Core capital and total risk weighted capital adequacy ratios of the Company stood at 10.21 percent and 15.27 percent respectively as at 31 December 2017. The information on minimum capital requirement is given on page 227.

Share Information

Information relating to earnings, net assets and market value per share is given in 'Financial Highlights' on page 6 Information on the trading of the shares and movement in the number of shares represented by the Stated Capital of the Company is given in the Section on 'Financial Capital' on pages 29 to 35.

Substantial Shareholdings

Information on Top Twenty Shareholders

Details of the top twenty shareholders percentages of their respective holdings and percentage holding of the public are given in the section on 'Financial Capital' on pages 32 to 33.

Directors

The names of the Directors who comprised the Board of Directors of the Company as at 31 December 2017 are given below and their attendance at the board meetings during the year is given on page 91 of the Annual Report.

| Name of the Director | Executive/ Non-Executive Status | Independent /Non-Independent Status |
|------------------------------|---------------------------------|-------------------------------------|
| Dr. S Lokuhewa | Chairman | |
| | Non Executive Director | Non-Independent |
| Mr. D M Gunasekara | Non Executive Director | Non-Independent |
| [resigned w.e.f. 27.04.2018] | | |
| Mr. W P R P H Fonseka | Non Executive Director | Non-Independent |
| Mr. K B S Bandara | Non Executive Director | Non-Independent |
| Mr. N Perera | Non Executive Director | Independent |
| Mr. S N Dayaratne | Non Executive Director | Independent |
| [Senior Director] | | |
| Mr. S P Arsakularatne | Non Executive Director | Independent |
| Mr. D M L B Dassanayake | Alternate Director to | |
| [resigned w.e.f. 27.04.2018] | Mr. D M Gunasekara | |
| Mr. R M D V Jayabahu | Alternate Director to Mr. | |
| [resigned w.e.f. 27.04.2018] | K B S Bandara | |

Appointments during the year under review

Mr. R M D V Jayabahu was appointed as Alternate Director to Mr. K B S Bandara - Non Independent /Non-Executive Director with effect from 20 April 2017

Mr. D M L B Dassanayake was appointed as Alternate Director to Mr. D M Gunasekara- Non Independent /Non-Executive Director with effect from 12 May 2017

Mr. S N Dayaratne was appointed as Senior Director to the directorate of MBSL in terms of Section 7(2) of the Finance Companies [Corporate Governance] Directions No. 3 of 2008 with effect from 28 December 2017 [He is a continuing director with effect from 26 July 2016].

Resignations during the year under review

Mr. C N Wijewardane resigned from the directorate of MBSL with effect from 10 August 2017.

Mr. H J D Fonseka resigned from the directorate of MBSL with effect from 28 September 2017.

Appointments after 1st January 2018

Mr. M P R Kumara was appointed as alternate director to Mr. W P R P H Fonseka with effect from 11 April 2018.

Resignations after 1st January 2018

Mr. D M Gunasekara resigned from the directorate of MBSL with effect from 27 April 2018.

Mr. D M L B Dassanayake resigned as alternate director to Mr. D M Gunasekara from the directorate of MBSL with effect from 27 April 2018.

Mr. R. M. D. V. Jayabahu resigned as alternate director to Mr. K B S Bandara from the directorate of MBSL with effect from 27 April 2018.

Recommendations for re-election

Mr. W P R P H Fonseka retire in terms of Article 86 read with Article 87 of the Articles of Association of the Company and being eligible for re-election have offered themselves for re-election at the forthcoming Annual General Meeting and are recommended by the Board of Directors.

Directors' Meetings

Details of Directors' meetings which

Annual Report of the Board of Directors on the Affairs of the Company

comprised Board meetings and Board Sub-Committee meetings namely Audit Committee, Integrated Risk Management Committee, Remuneration Committee and Related Party Transactions Review Committee are presented on page 91.

Interests Register

In compliance with the provisions of the Companies Act No.7 of 2007, an Interests Register is maintained by the Company.

The Company's Directors have made general declarations in relation to their respective interests in transactions/ proposed transactions with the Company as provided for in section 192(2) of the Companies Act No.7 of 2007. Arising from these, details of contracts in which the Directors' have an interest are given under Note 41 to the Financial Statements on page 196 to 197 of the Annual Report, dealing with related party disclosures.

Directors' Remuneration

Directors' fees and emoluments paid during the year are as follows:

| | Company Rs.Mn | Group Rs.Mn |
|-----------------------------------|------------------|----------------|
| Directors' Fees and Emoluments | 6.30 | 6.67 |

Directors' Interest in Shares of the Company

None of the Directors of the Board held shares in the Company as at 31 December 2017.

Directors' Interests in Contracts or Proposed Contracts

Directors' interests in contracts or proposed contracts with the Company, both direct and indirect are disclosed on pages 196 to 197.

Related Party Transactions

The Company has complied with the

requirements of the listing rules of the Colombo Stock Exchange on Related Party Transactions. Directors have disclosed transactions if any that could be classified as related party transactions in terms of Sri Lanka Accounting Standard - LKAS 24 - 'Related Party Disclosures', which is adopted in preparation of the Financial Statements. This Disclosure is given in Note 41 to the Financial Statements on pages 196 to 198 which form an integral part of the Annual Report of the Board of Directors.

Appointment of Auditors

The retiring Auditors, the Auditor General have expressed their willingness to continue in office for the financial year 2018.

A resolution to re-appoint the Auditor General and to authorize the Directors to determine their audit fees will be proposed at the forthcoming Annual General Meeting.

Auditors' Remuneration and Interests in the Company / Group

The Auditors, Auditor General were paid Rs. 1,880,884 for the year ended 31 December 2017 as audit fees by the Company. In addition, they were paid Rs. 652,000 by the Company, for permitted non-audit-related services.

The external audit is carried out by the Auditor General in terms of the constitution of the country. The Auditor General was assisted by the M/s BDO Partners, Chartered Accountants during the year 2017.

As far as the Board of Directors are aware, the Auditors do not have any other relationship or interests in the Company or its Subsidiary or Associate.

Compliance with Laws and Regulations

The Company has not engaged in any activity contravening any laws and regulations.

Environmental Protection

The Company has used its best endeavors to comply with the relevant environmental laws and regulations. The Company has not engaged in any activity that is harmful or hazardous to the environment.

Corporate Donations

During the year under review, the Company has made donations amounting to Rs. 38,130 [2016 - Rs.197,286] in terms of the resolution passed at the last Annual General Meeting. This amount excludes contributions made towards the Company's Corporate Social Responsibility initiatives. The CSR initiatives of the Company are presented in Social and Relationship Capital Report given on pages 47 to 48 of this Annual Report.

Events After The Reporting Period

Details of events after the reporting period are reflected in Note 43 to the Financial Statements on page 201.

Outstanding Litigation

In the opinion of the Board of Directors and the Company's lawyers, pending litigation against the Company disclosed in Note 47 to the Financial Statements on page 206 will not have a material impact on the financial position of the Company or on its future operations.

Going Concern

The Board of Directors have a reasonable expectation that the Company possesses adequate resources to continue in operation for the foreseeable future. For this reason, the Board of Directors continue to adopt the going concern basis in preparing Financial Statements even though, Subsidiary Company, MBSL Insurance Company Limited (MBSLI) has issues with reference to the going concern of the Company [MBSLI] as discussed in the Note 44 to the Financial Statements on page 202.

Risk Management And System Of Internal Controls

Risk Management

The Company has an ongoing process in place to identify, evaluate and manage the risks that are faced by the Company. The Directors continuously review this process through the Board Integrated Risk Management Committee. Specific steps are taken by the Company in managing risks are detailed in the Risk Management Report on pages 105 to 114.

Corporate Governance

Directors' Declarations

The Board of Directors declare that-

- (a) The Company complied with all applicable laws and regulations in conducting its business and have not engaged in any activity contravening the relevant laws and regulations.
- (b) The Directors have declared all material interests in contracts involving the Company.
- (c) All endeavors have been made to ensure that the Company's shareholders have been treated equitably in accordance with the original Terms of Issue.
- (d) The business operates as a going concern with supporting assumptions or qualifications as necessary, and that the Board of Directors has reviewed the Company's Corporate/ Business plans and is satisfied that the Company has adequate resources to continue its operations in the foreseeable future. Accordingly, the Financial Statements of the Company, its Subsidiary and Associate Company are prepared based on the going concern concept, and
- (e) The Directors have conducted a review of internal controls covering financial, operational compliance and risk management and have obtained a reasonable assurance of their effectiveness and successful adherence herewith.

The measures taken and the extent to which the Company has complied with the Codes of Best Practices on Corporate Governance issued by The Institute of Chartered Accountants of Sri Lanka and the Securities and Exchange Commission of Sri Lanka, the Colombo Stock Exchange and the Central Bank of Sri Lanka are given in the Section on 'Corporate Governance' on pages 62 to 91.

Human Resources

The Company continued to implement appropriate Human Resource Management Policies to develop employees and optimize their contribution towards the achievement of corporate objectives. These policies and procedures ensure the equitable treatment of all employees which has resulted in high motivation.

Annual General Meeting

The Thirty Sixth Annual General Meeting of the Company will be held at the Grand Ballroom, Galadari Hotel, No. 64, Lotus Road, Colombo 01 on 26 June 2018 at 10.00am. The Notice convening the Thirty Sixth Annual General Meeting is given on page 262.

Acknowledgement of the Contents of the Report

As required by Section 168 [1] [k] of the Companies Act No. 07 of 2007, the Board of Directors hereby acknowledge the contents of this Annual Report.

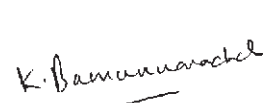
This Annual Report is signed for and on behalf of the Board of Directors by:



Dr. S Lokuheva
Chairman



K B S Bandara
Director



K Jayatilake
Company Secretary

17 May 2018
Colombo

Audit Committee Report

The Audit Committee of the Merchant Bank of Sri Lanka & Finance PLC (MBSL) functions in terms of the Audit Committee Charter approved by the Board of Directors. The scope of the Audit Committee Charter is reviewed and updated regularly incorporating the provisions of the new regulatory requirements, standards and Acts

Composition of Audit Committee

The composition of the Audit Committee is as follows:

- Mr. W.P. Russel Fonseka – Chairman
Non Executive
Non Independent Director
[Appointed with effect from 10/08/2016]
- Mr. K.B.S Bandara – Member
Non Executive
Non Independent Director
[Appointed with effect from 10/08/2016 and resigned with effect from 23/12/2016 and reappointed on 24/01/2017 by the reconstitution of the Audit committee by the Board on its 513th Board Meeting held on 24/01/2017]
- Mr. Niroshana Perera – Member
Non Executive
Independent Director
[Appointed with effect from 10/08/2016]
- Mr. S.N. Dayaratne – Member
Non Executive
Independent Director
[Appointed with effect from 10/08/2016]

- Mr. S. Arsakularatne – Member
Non Executive
Independent Director
[Appointed with effect from 10/08/2016]
- Mr. H.J.D. Fonseka – Member
Non Executive
Independent Director
[Appointed with effect from 23/12/2016 and resigned on 28/09/2017]

The Committee Meetings

The Committee held 12 meetings during the year under review. The proceedings of the Audit Committee are reported regularly to the Board of Directors.

The Chief Executive Officer, Head of Finance, attend the meetings by invitation. The Heads of Divisions were invited to the meetings of the Committee at various times to get clarifications.

Assistant General Manager – Internal Audit is the Secretary to the Committee

Key Responsibilities of the Committee

Audit Committee of the MBSL which functions as a subcommittee of the Main Board, assists the Main Board in fulfilling its oversight responsibilities and provides an independent review of the financial reporting process. The following areas come under the purview of the Audit Committee;

Financial Reporting

- a) Reviews the financial information of the company in order to ensure the integrity of the financial statements, its annual report, accounts etc.
- b) Evaluating, reviewing and monitoring the adequacy and effectiveness of the internal control systems to ensure integrity of the financial reporting.

Compliance

- a) Reviews the effectiveness of the systems and procedures adopted by the company and monitors compliance with applicable laws and regulations.
- b) Reviews the findings of the examinations carried out by regulatory agencies and/or any auditor on compliance with such laws and regulations.
- c) Follows-up of any instances of non-compliance with statutory and regulatory requirements

Internal Audit

- a) Reviews of performance of the Internal Audit Function, audit reports and follow up on recommendations
- b) Reviews the audit charter, audit plans, activities, audit scope, reporting requirements, etc. of the internal audit function of the company
- c) Reviews findings and recommendations by the Internal Auditors, together with comments made by Management
- d) Assesses the effectiveness of such findings and responses.

External Audit

- a) Evaluates the independence and objectivity of the External Auditors and the effectiveness of the audit process
- b) Coordination with Internal Audit.
- c) Reviews the External Audit Report on the financial statements and Management Letter outlining the findings, observations and recommendations and management responses and the status of any corrective action plans.

- d) The Committee meets the External Auditors separately to discuss any matters that the Committee or Auditors believe should be discussed privately.

Summary of the Activities carried out by the Committee during the year

During the year under review the Committee discharged its duties as follows;

Financial Information

- a) The quarterly and annual financial statements of the Company were reviewed and discussed with the Management and the External Auditors, prior to dissemination to the public, including the extent of compliance with Sri Lanka Accounting Standards and the adequacy of disclosures required by other applicable laws, rules and guidelines.
- b) Evaluated the adequacy and effectiveness of internal control systems to ensure integrity of the financial reporting

Compliance:

- a) Reviewed the effectiveness of the systems and procedures of the company to monitor compliance with applicable laws and regulation of the country.
- b) Reviewed the reports submitted by the Management on the state of compliance with the relevant laws, regulations and settlement of statutory payments was reviewed and discussed.

Internal Audits

- a) Assigned the Internal Auditor at regular intervals to review effectiveness of the internal control procedures, accounting systems and operations procedures of the organisation.

- b) Reviewed the reports received from the Internal Auditor covering audits and investigations and discussed with the Management on the recommendations made and followed up on the implementation.
- c) Reviewed the Internal Audit programmes to ensure that implementation of internal control is monitored and their adequacy is assessed on a continuous basis.
- d) Reviewed the Internal Audit reports and monitored the implementation of recommendations made therein.

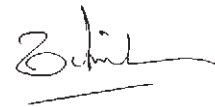
External Audit

- a. The external audit is carried out by the Auditor General in terms of the Constitution of the Country. The Auditor General was assisted by the M/s BDO partners, Chartered Accountants during the year 2017. Prior to commencement of the Audit, the Audit Committee met with the External Auditors, M/s BDO partners to review and discuss the process and procedures.
- b. The Committee reviewed the Management Letter issued by the External Auditors and the Management response thereto.
- c. Reviewed and followed up upon final audit issues identified by the Auditors pertaining to the audit for the year 2017

Conclusion

The Audit Committee is satisfied that internal controls which provide a reasonable assurance that the affairs of the company are managed in accordance with approved policies of the company and that the company's assets are properly accounted for and adequately safeguarded.

The Audit Committee confirms that the responsibilities of the Audit Committee in terms of the Direction No.4 of 2009 on Corporate Governance issued by the Central Bank and the Listing Rules of the Colombo Stock Exchange have been complied with.



W P R P H Fonseka
Chairman - Audit Committee

29 March 2018
Colombo, Sri Lanka

Remuneration Committee Report

The Remuneration Committee is a sub-committee of the Board of Directors comprising of the following members.

Effective from 23 Dec. 2016 the Remuneration Committee comprises as follows:

Dr. Sujeewa Lokuheewa – Chairman/ Non Independent Non Executive Director

Mr. C N Wijewardane – Non Independent/ Non Executive Director

[resigned from the directorate of MBSL with effect from 10.08.2017]

Mr. Niroshana Perera – Non Independent/ Non Executive Director

Mr. H J Denzil Fonseka – Independent/Non Executive Director

[resigned from the directorate of MBSL with effect from 28.09.2017]

Mr. S N Dayaratne – Independent/Non Executive Director

Mr. S P Arsakularatne – Independent/Non Executive Director

Effective from 28.12.2017 the Remuneration Committee comprises as follows:

Dr. Sujeewa Lokuheewa – Chairman/ Non Independent Non Executive Director

Mr. S N Dayaratne – Independent/Non Executive Director [Senior Director]

Mr. D M Gunasekara – Non Independent/ Non Executive Director

[resigned from the directorate of MBSL with effect from 27.04.2018]

Mr. Niroshana Perera – Independent/Non Executive Director

Mr. S P Arsakularatne – Independent/Non Executive Director

The Chairman of the Remuneration Committee was also functioning as the Chairman of the Board of Directors.

The Remuneration Committee of Merchant Bank of Sri Lanka & Finance Plc is responsible to determine a broad remuneration framework for the Chairman and the Board of Directors including the Executive (if any) and Non-Executive Directors as well as the Chief Executive Officer.

The Remuneration Policy of the Company endeavours to attract, motivate and retain quality management in a competitive environment with the relevant expertise to achieve the desired objectives of the Company.

In addition to taking into account the long term interest of MBSL and its shareholders, the Remuneration Committee is required to comply with any circulars pertaining to Public Enterprises [Public Finance Enterprises Circulars], any Directions issued by the relevant line Ministry and the concurrence of the Bank of Ceylon in determining the remuneration paid to the Directors.

The Directors are entitled for fees for attendance at Board Meetings and sub-committee meetings [per sitting] and also a reimbursable travelling allowance. Further, the members are also entitled for the payment of additional fees for any additional services/responsibilities taken by them through committee level participation as may be determined from time to time.

The remuneration of the Chairman shall be determined by taking into account his/ her relevant experience, academic and competency levels, leadership qualities and having regard to competitive market rates paid by similar institutions.

The remuneration of the CEO shall be determined based on his/her industry experience, academic and competency levels, leadership credentials, competitive market rates paid by similar institutions and any other relevant factors as may be determined by the Remuneration Committee/Board in line with the remuneration structure of the organization .

The remuneration of the CEO may comprise of different components such as cash and non-cash benefits and will be linked to measurable standards of performance.

The Remuneration Committee makes its recommendations to the Board of Directors for final approval.

The total Directors' emoluments are disclosed in Note 13 on page 146 of the Financial Statement.



Dr. Sujeewa Lokuheewa
Chairman

Remuneration Committee

17 May 2018
Colombo

Related Party Transactions Review Committee Report

Purpose of the Committee

The purpose of the Committee is to review in advance all proposed related party transactions other than those transactions explicitly exempted in the Code. Accordingly, except for transactions mentioned under Rule 27 of the Code, all other related party transactions are required to be reviewed by the Committee either prior to the transaction being entered into or, if the transaction is expressed to be conditional on such review, prior to the completion of the transaction.

Composition of the Committee

The Related Party Transactions Review Committee is appointed by the Board of Directors of the Company. As at 31 December 2017, it comprises of the following Directors:

| | Name of the Directors | Directorship Status | Membership Status |
|---|------------------------|--|-------------------|
| 1 | Mr. S.N Dayaratne | Non Executive Independent Director | Chairman |
| 2 | Mr. W.P.R.P.H Fonseka | Non Executive Non Independent Director | Member |
| 3 | Mr. K.B.S Bandara | Non Executive Non Independent Director | Member |
| 4 | Mr. S. P Arsakularatne | Non-Executive Independent Director | Member |
| 5 | Mr. N. Perera | Non-Executive Independent Director | Member |

Scope of the Committee

- Adopting policies and procedures to review related party transactions of the Company and reviewing and overseeing existing policies and procedures.
- Reviewing in advance all proposed related party transactions of the Company except those explicitly exempted in the Code under Rule 27
- Determining whether related party transactions that are to be entered into by the Company require the approval of the Board or Shareholders of the Company
- Establishing guidelines in respect of recurrent Related Party Transactions to be followed by the Corporate Management in respect of ongoing dealings with the relevant related party
- Ensuring that no Director of the Company shall participate in any discussion of a proposed Related Party Transaction for which he or she is a related party, unless such Director is requested to do so by the Committee for the express purpose of providing information concerning the Related Party Transaction to the Committee
- Ensuring that immediate market disclosures and disclosures in the Annual Report as required by the applicable rules/regulation are made in a timely and detailed manner

Policies and Procedures

The Company has in place a Related Party Transactions Policy [RPTP] whereby the categories of persons/entities who shall be considered as "related parties" has been identified. The RPT Policy ensures that the Company does not engage in transactions with related parties in a manner that would grant related parties "more favorable" treatment.

In accordance of the RPT Policy, self-declarations are obtained from each Director for the purpose of identifying parties related to them.

The Code of Business Conduct and Ethics of the Company, which sets out internal policies applicable to conflicts of interests, also plays a key role in managing Related Party Transactions.

Meetings of the Committee

The Committee met twice during the year under review. The quorum for a meeting is four members. Members of the Corporate Management were invited to participate in the meeting of the Committee as required. The Finance Division submitted comprehensive reports on Related Party Transactions to the Committee

Related Party Transactions for the Year 2017

Details of all transactions with the related parties during the year 2017 were reviewed by the Committee. There were no non-recurrent or recurrent related party transactions that exceeded the respective thresholds mentioned in the Listing rules of the Colombo stock exchange.

Details of the related party transactions are disclosed under Note 41 on pages 196 to 198 of the Financial Statements.

Related Party Transactions Review Committee Report

Declaration

The declaration by the Board of Directors that no related party transaction falling within the ambit of the Listing Rules was entered into by the Company during 2017 is contained in the Annual Report of the Board of Directors on the Affairs of the Company on pages 92 to 97.



S.N Dayaratne

Chairman

Related Party Transactions Review
Committee

17 May 2018
Colombo

Integrated Risk Management Committee Report

The Integrated Risk Management Committee (IRMC) of the Merchant Bank of Sri Lanka & Finance PLC (MBSL) functions in terms of the Risk Management Policy approved by the Board of Directors. The Risk Management Policy is reviewed and updated regularly in order to maintain prudent risk management practices within the Company.

The IRMC Meetings

The IRMC held 6 meetings during the year under review. The Risk Assessment Reports, Risk Management Policies, Compliance Reports and other risk related reports are reviewed at the IRMC meeting and Risk Management Policies and Risk Assessment Reports are forwarded to the Board of Directors with recommendation as specified by the corporate governance directions issued by the Central Bank of Sri Lanka (CBSL).

Composition of Integrated Risk Management Committee

| Name | Designation |
|--|--|
| Board Level Members | |
| Mr. K.B.S Bandara | Chairman of the IRMC Non-Executive Non Independent Director |
| Mr. N.Perera | Non-Executive Independent Director |
| Mr. S N Dayaratna | Non-Executive Independent Director |
| Mr. C.N. Wijewardane* | Non-Executive Non Independent Director |
| Mr. H.J.D. Fonseka** | Non-Executive Independent Director |
| Management Level Members | |
| Mr. Nishaman Karunapala | Chief Executive Officer |
| Mr. Duleep Daluwatta | COO/ Head of CA& CM and Real Estate |
| Ms. Shyamalie Amaratunga | SDGM / Compliance Officer |
| Ms. Karnika Jayatilake | Company Secretary/DGM -Legal |
| Mr. Chamara Withanachchi | Head of IT |
| Mr. Purna Kandanaarachchi | Head of Finance |
| Mr. Senaka Uduwawala | DGM - Range 2 & Region 4 |
| Mr.Jude Gamalath | DGM-Marketing & Product Development, Region 2 |
| Mr.Kumudu Jayasundara | AGM-Recoveries |
| Mr.Himala Wijayatunga | Manager -Risk Management |
| * Resigned with effect from 10 August 2017 | |
| ** Resigned with effect from 28 September 2017 | |

Key Responsibilities of the Committee

IRMC is a Board appointed subcommittee consist of three non-executive directors, CEO and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The Company Secretary of MBSL acts as the secretary to the committee.

IRMC works with key management personnel closely and make decisions on behalf of the Board within the framework of the authority and responsibility assigned to the committee.

In addition to that the committee is responsible for;

- (I) Assess all risks to the Company on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on the Finance Company basis and group basis.
- (II) Review the adequacy and effectiveness of all management level committees such as the credit committee and the asset-liability management committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the committee.
- (III) Take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the committee on the basis of the Company's policies and regulatory and supervisory requirements.
- (IV) Meet at least quarterly to assess all aspects of risk management including updated business continuity plans.
- (V) Take appropriate actions against the officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the committee, and/or as directed by the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka.
- (VI) Submit a risk assessment report within a week of each meeting to the Board seeking the Board's views, concurrence and/or specific directions.

Integrated Risk Management Committee Report

[VII] Establish a compliance function to assess the Company's compliance with laws, regulations, directions, rules, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the committee periodically.

Conclusion

The Committee has reviewed the process of identification, evaluation and management of all significant risks of MBSL and supported execution of the overall business strategy of the company within predefined risk parameters.

Gratitude

The Committee wishes to express its sincere gratitude to Mr.C.N. Wijewardane and Mr. H.J.D. Fonseka for their valuable contribution to the Committee during their tenure.



K.B.S Bandara

Chairman
Integrated Risk Management Committee

17 May 2018
Colombo

Risk Management

While growth is fundamental to our success, proactive risk management is vital to guiding strategy in a manner that balances risk and return considerations. The Company’s risk management framework embodies robust policy frameworks, clearly defined governance structures, mitigating strategies and ongoing monitoring.

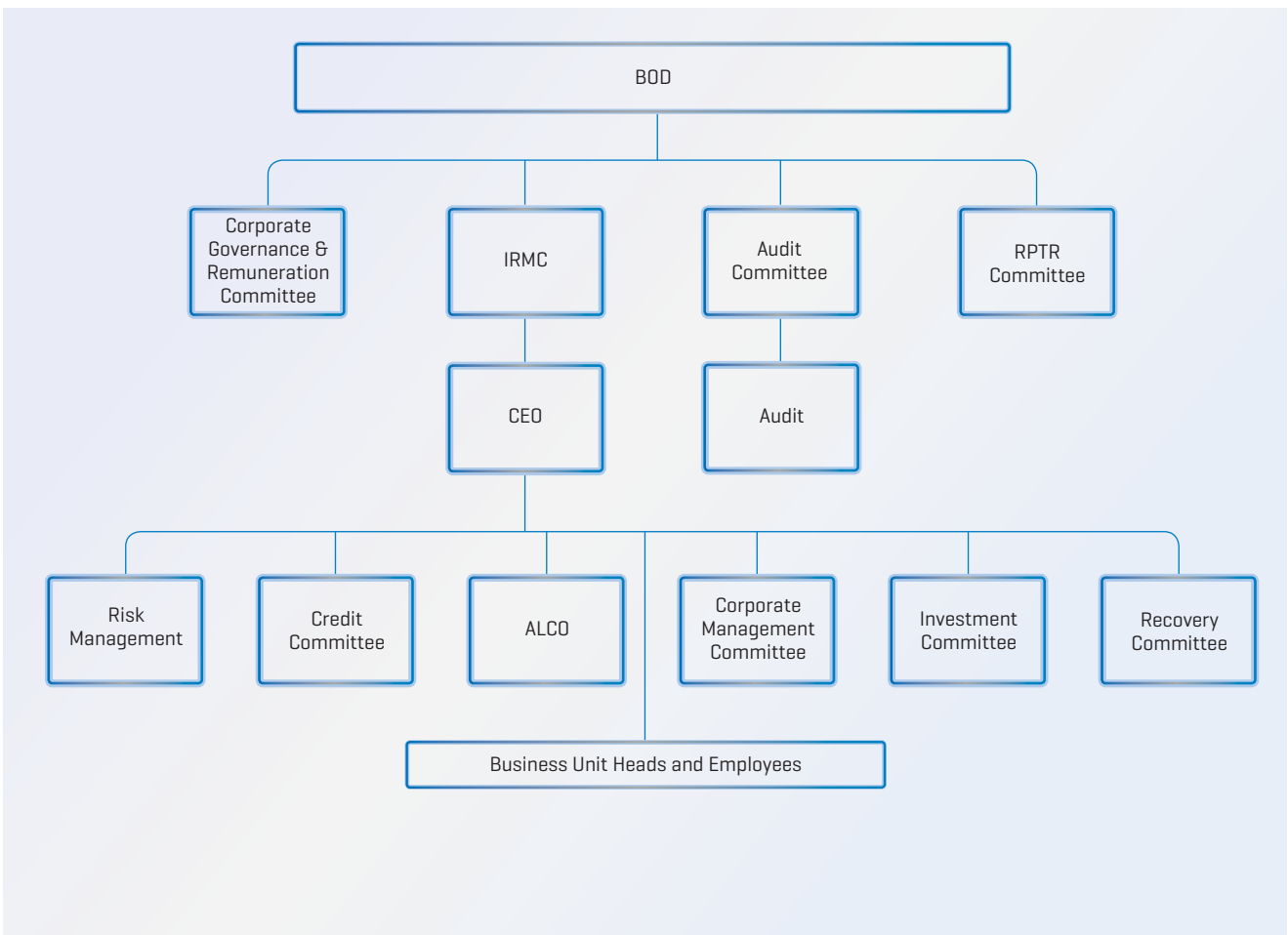
Risk Governance and Approach

The Company adopts the globally accepted three line of defense model, which clearly defines responsibilities for risk management. Risk identification, assessment, evaluation and assurance are subdivided to three lines in the organizational hierarchy with clearly defined roles and responsibilities. Operational managers are involved in risk identification and assessments while risk evaluation and monitoring activities are performed by independent risk functions

of the organization. Risk assurance is the third line and evaluates the adequacy of internal controls.

The structured and formalized approach towards risk management enables the Board of Directors to determine risk appetites and approve risk strategies that are aligned to the Company’s broader business objectives. The Integrated Risk Management Committee provides independent oversight of all risk related aspects across the Group and works

closely with the management in ensuring that adequacy and effectiveness of the implementation of risk governance structures, policy frameworks, standards and processes. The Committee consists of three non-executive directors, CEO and key management personnel supervising risk categories, i.e., credit, market, liquidity, operational and strategic risks. The terms of references and committee activities during the year are detailed in the IRMC Report on page 103 of this Annual Report.



Risk Management

Executive level committees engaged in risk management related functions are listed below;

| Committee | Composition | Roles and responsibilities |
|---|--|--|
| Credit Committee | Corporate management personnel headed by the CEO | <ul style="list-style-type: none"> Ensuring that the Group's credit risk exposures are managed within the Board approved risk appetite. Approving credit within the delegated parameters (assigned by the BOD) subject to specific terms and conditions. Recommending specific policies and procedures that require the attention of the BOD. |
| Asset Liability Management Committee | Board appointed management committee headed by the CEO. | <ul style="list-style-type: none"> The Committee is responsible for the management of Market Risk, Liquidity Risk and the management of balance sheet structures including Capital Risk. |
| Investment Committee | Headed by the CEO and represented by corporate management personnel | <ul style="list-style-type: none"> Managing the Company's investment portfolio and making decisions pertaining to the purchase, hold and selling of investments. |
| Recovery Committee | Consists of corporate management members and headed by CEO | <ul style="list-style-type: none"> Responsible for implementing the collections and recovery strategies. Ensuring that the NPL position is maintained within defined parameters. |
| IT Steering Committee | Headed by the CEO and include one representative from each division. | <ul style="list-style-type: none"> Ensuring that the Group's IT strategy is aligned to the growth strategies and business requirements of each division. |

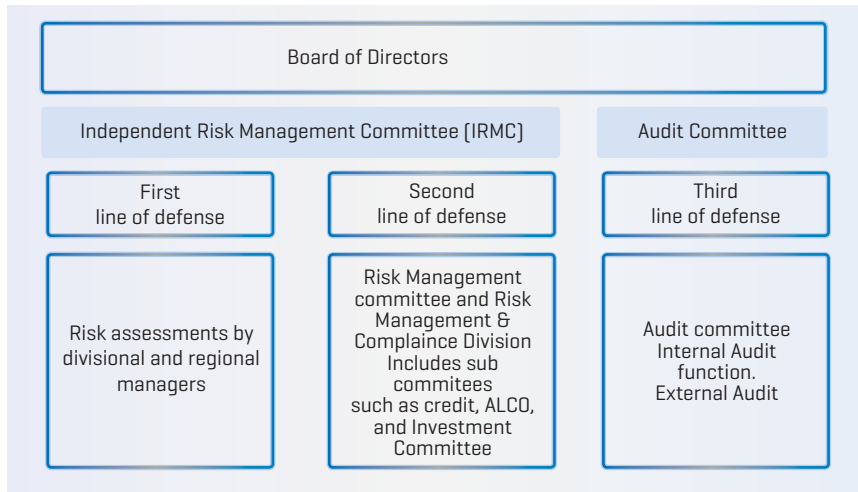
Risk Monitoring and assurance

Risk assessment reports are reviewed every quarter by IRMC and identified risk indicators are evaluated every month. Routine meetings are held with six sub committees on risk evaluation. The Audit Committee appoints an internal auditor to perform a detailed risk assessment every year with an audit plan for perusal by the Board of Directors. Additionally, the external Audit is undertaken by the Auditor general of Sri Lanka where the independence is guaranteed under the Constitution of Sri Lanka hence the audit committee has no role to play in the engagement of the external auditor.

Risk Framework

1. Policies: MBSL has a comprehensive suite of risk policies that address the principal risks of the organization including credit policies, whistleblower policies, impairment policies and provision policies.
2. Internal controls: segregation of duties and clearly defined authority lines have been implemented across all core business functions and operations including credit approval, recovery and monitoring among others.
3. Risk appetite
4. Risk based culture within the organization

MBSL Three lines of defense model



Principal Risk Categories

Risk arises from all aspects of the external operating landscape and internal operations and processes. External variables including economic growth, regulations, government policies and customer preferences impact asset growth, cost management, profitability and credit recovery of the company. In the meantime, effectiveness and efficiency of our resources such as technology, people and process impact strategy implementation and ability of the Company to pursue growth and service excellence.

Principal risks in 2017



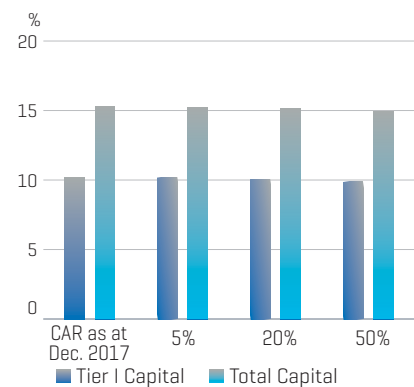
| Credit Risk | Potential Impact | Risk Mitigation Techniques |
|--|---|---|
| <p>Potential losses arising from any clients or market counterparties fails to fulfil their contractual obligations to MBSL. Credit Risk takes the form of default risk and concentration risk.</p> <ul style="list-style-type: none"> Default Risk is loss incurred on customer defaults Concentration Risk is the over dependence on a single customer, product or sector. | <ul style="list-style-type: none"> Increase in Non-performing loans. Loan write offs Increasing impairments and provisioning affecting profitability | <ul style="list-style-type: none"> Stringent pre -credit sanctioning and post credit sanctioning. KPIs for credit recovery officers. Monitoring of risk indicators. Structured credit recovery process. |

Credit risk

Materiality

As a lending organization, credit risk is among the Company’s principal risk exposures. Stress testing evaluates the vulnerability of the Company to credit risk and results in 2017 indicated that the capital strength of the organization could withstand a 28% increase in non-performing loans provision during the year.

Credit Risk



Oversight

The range heads and branch managers are responsible for maintain the Company’s credit quality. The business units function as the first line of defense in managing credit risk, supported by independent review by the Credit Committee, as well as the processes, standards and frameworks implemented by the Risk Management Division.

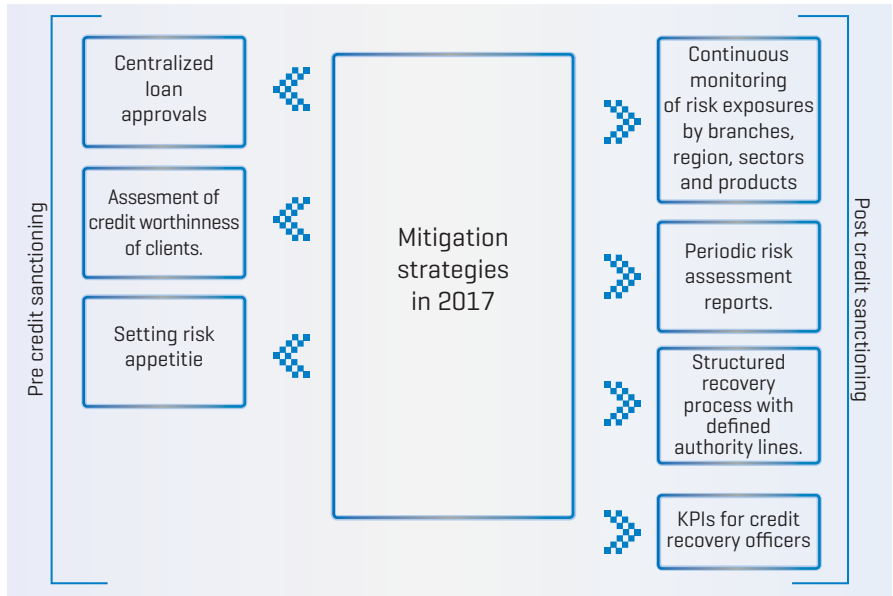
Risk Management

Risk Mitigation in 2017

The Company has implemented numerous pre and post-credit mechanisms to ensure that credit quality is maintained within defined parameters. During the year under review, strategic focus was placed on strengthening credit quality with intense training initiatives being carried out to nurture a culture of risk-awareness among employees, particularly the credit staff. Key improvements made during the year are listed below;

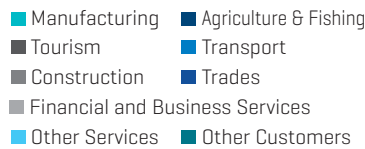
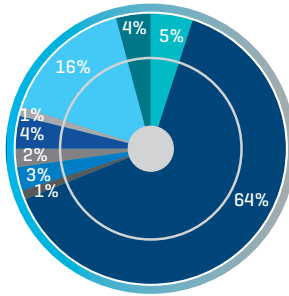
- Introduced a comprehensive credit inspection report which ensures deeper engagement between the credit appraisal officer and customer
- Adopted a collateral-based approach to lending
- More proactive approach towards collections and monitoring
- Discontinued certain product segments which were showing increased delinquencies, particularly unsecured lending
- Streamlined recovery mechanisms
- Increased penetration in the two-wheeler and biking loan segments

Furthermore, the credit exposures of the Company by sector, product and customer are continuously evaluated to proactively minimize concentration risk.

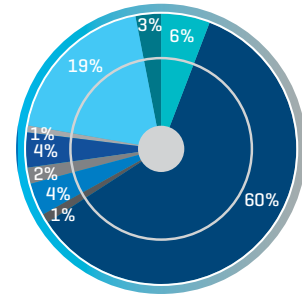


Risk indicators

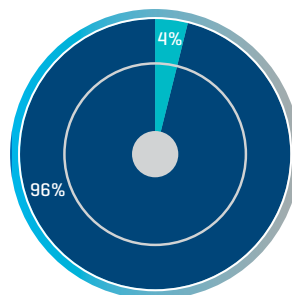
Sector Wise Analysis 2017



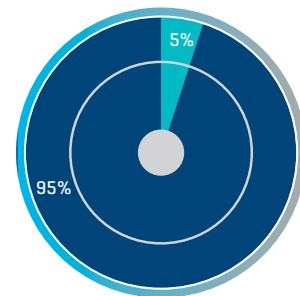
Sector Wise Analysis 2016



Customer Wise Analysis 2017



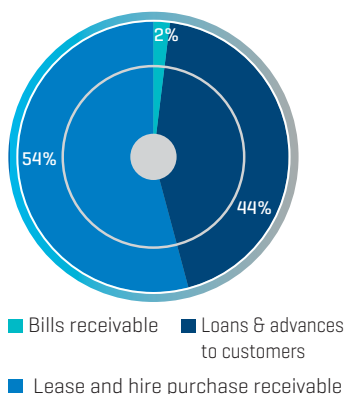
Customer Wise Analysis 2016



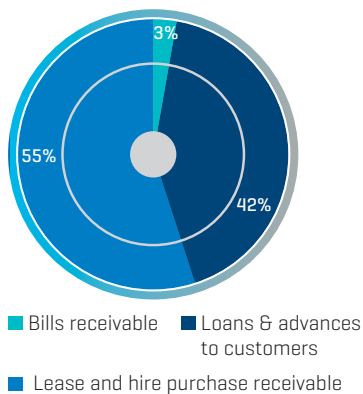
Concentration risk

The Company maintained a well-diversified customer base across sectors, products and customer groups. By name, the 20 largest customers accounted for only 4% of the lending portfolio. With regards to sectorial composition, the credit exposure to service sector was curtailed during the year, while increased focus was placed on two and three-wheeler financing and gold loan portfolios. Concentration on Leasing and HP products were increased since the company more focused on securitized lending.

Product Composition 2017



Product Composition 2016



Non -performing loans [NPL]

The Company's NPLs increased during the year, reflecting moderating economic conditions, a subdued agriculture sector and relatively lax credit underwriting in the past. Recovery mechanisms were also streamlined and strengthened during the year, with clearly defined responsibilities, stronger customer engagement and introduction of credit recovery KPIs.

Market Risk

| Market Risk | Potential Impact | Risk Mitigation |
|---|--|--|
| <p>Potential loss due to changes in market variables including:</p> <ul style="list-style-type: none"> Interest rate risk Equity risk due to share price movements. Commodity risk due to fluctuations in gold prices. | <ul style="list-style-type: none"> Pressure on Net interest margins. Re-pricing of assets and liabilities. Mark to market gains/ losses on equity portfolio. Decline in value of collateral held for gold loans. | <ul style="list-style-type: none"> Continuous monitoring of market variables. Prudent Loan to value ratios for gold loans. Diversification to other business areas such as corporate advisory that generate non-interest incomes. |

Oversight

The ALCO holds executive responsibility for overseeing the Company's market risk which includes monitoring interest rate, commodity and equity risks. Key market variables such as interest rates, gold prices and share price movements are continuously monitored. Based on the risk appetite of the Company and movements in market variables, the ALCO and Investment committees focus on re-aligning lending and investment portfolios, refining lending limits and evaluate the sensitivity to market risk. The Company has the capacity to withstand an 50% shock of market risk without capital adequacy ratio being below regulatory requirements.

| CAR ratio | Shock Level | | | |
|------------------------|-------------|--------|--------|--------|
| Tier 1 CAR at year end | 10.21% | 5% | 20% | 50% |
| Equity Risk | 10.21% | 10.21% | 10.21% | 10.20% |
| Commodity risk | 10.21% | 10.21% | 10.21% | 10.21% |

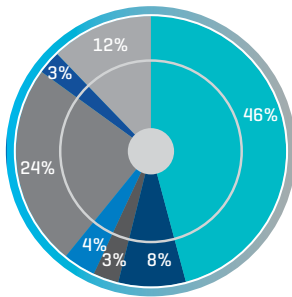
Equity Risk

Equity markets rebounded during the year as reflected by the recovery of the All Share Price Index (ASPI) by Sept 2017 after three consecutive years of declining growth. Economic growth and improving external trade activity in 2017 encouraged foreign investors to invest in Sri Lankan equity markets enhancing market performance.

During the year, the Company further reduced its exposure to equity investments to Rs. 231.26 million [0.65% of total assets], compared to Rs. 323.66 million [1% of total assets] the year before. We generated mark to market gains of Rs.5.62 million on the equity portfolio; the Company's portfolio continues to be well diversified with balanced exposure across all industry sectors.

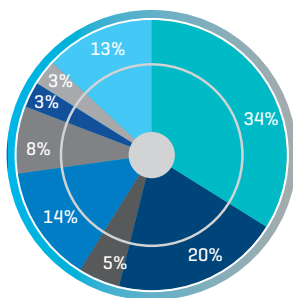
Risk Management

Sector Portfolio 2017



- Banks/Finance & Insurance
- Beverage Food & Tobacco
- Construction & Engineering
- Diversified Holdings
- Hotels & Travels
- Investment Trust
- Manufacturing

Sector Portfolio 2016



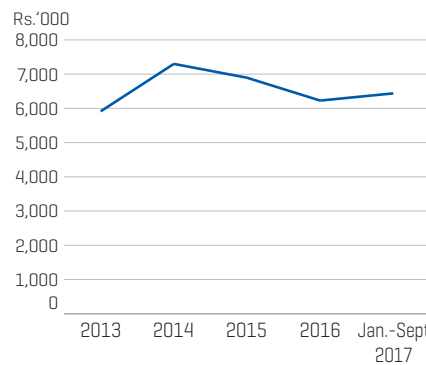
- Banks/Finance & Insurance
- Hotels & Travels
- Diversified Holdings
- Investment Trust
- Construction & Engineering
- Beverage Food & Tobacco
- Plantation

Commodity risk

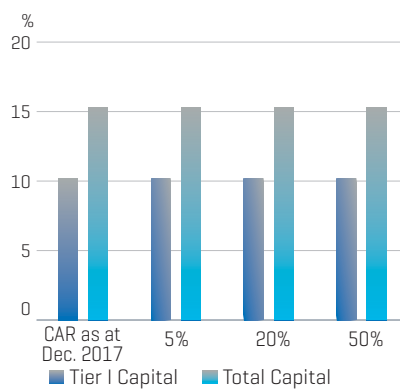
The Company's exposure to commodity risk stems primarily from gold price movements. Global gold prices increased in end of 2017, supported by the overall improvement in global commodity prices. MBSL increased its exposure to gold loans during the year, expanding its portfolio by nearly 40% to Rs.699.63 million. Parallel to portfolio growth we also strengthened our risk management practices in the segment through adopting the following measures;

- Enhanced the internal audit function for physical verification of gold items
- Regular branch visits by corporate management
- Increased training for pawning officers
- Maintenance of loan to value ratio averaging 75%

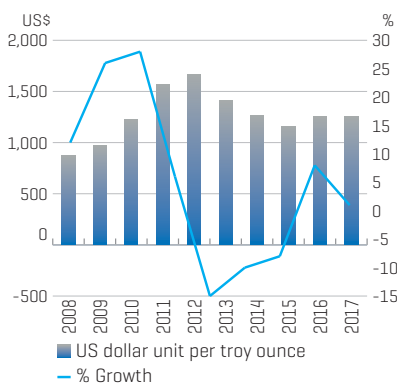
Movement in ASP Index Value



Market Risk -Pawning

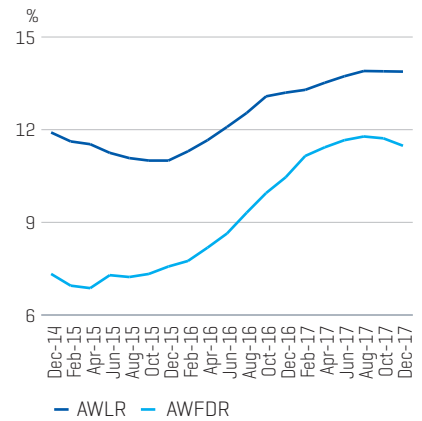


Gold Prices

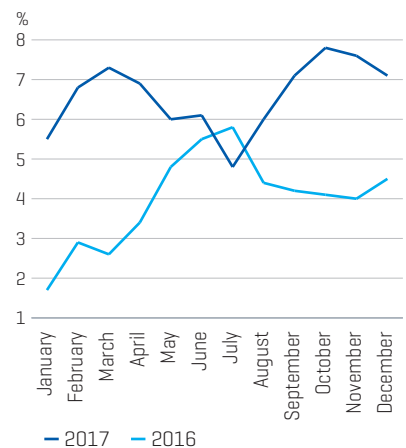


Interest rate risk

Interest Rates



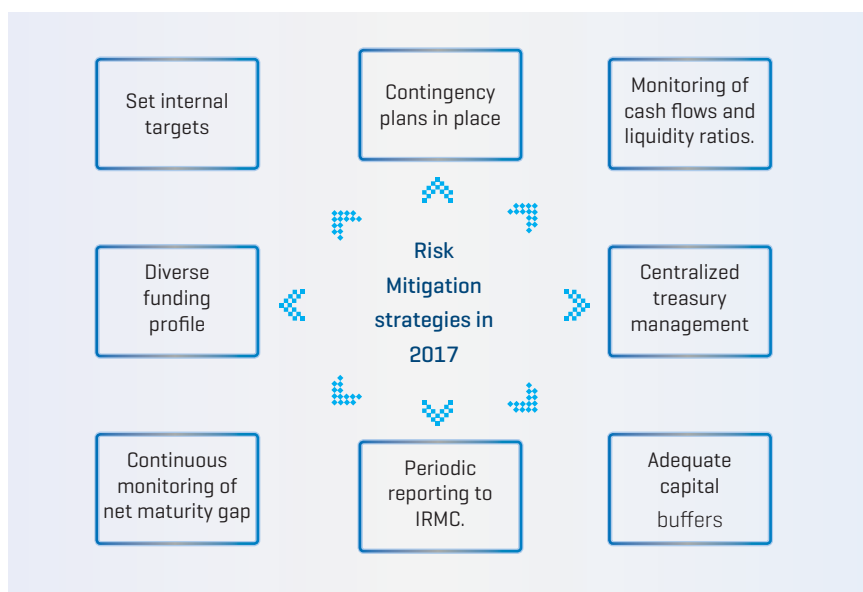
Inflation-CCPI



Liquidity and Funding risk

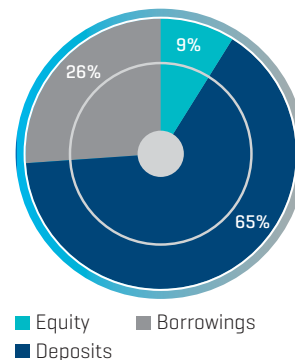
| Liquidity Risk | Potential Impact on | Risk mitigation |
|---|--|---|
| Financial loss arising from the Company's ability to dispose its assets/liabilities in a timely manner to meet the obligations that fall due. | <ul style="list-style-type: none"> Market risk Assets value Cost of funding and profitability Reputation Trust and confidence of depositors. Cash flow management. | <ul style="list-style-type: none"> Monitor the maturity mismatch between interest bearing assets and liabilities. Maintain adequate liquidity and capital buffers. Diversified funding base. Maintain liquidity ratios above stipulated limits. Continuous monitoring of cash flows. |

The liquidity risk is managed by the ALCO and treasury functions that ensure the Company has adequate liquidity at any given time. Being one of the core risks of any financial institution, MBSL implements sound contingency plans and maintains adequate capital buffers in addition to risk mitigation initiatives. During the year, the Company strengthened its Tier 1 capital base with the debenture issue of Rs. 2 Bn with a maturity of 5 years. Total CAR ratios strengthened during the year to 15.27% compared to 10.69% last year and remains in line with regulatory requirements. In addition, unused credit lines amounted to Rs. 3.3 Bn.



The Group also maintains a relatively diverse funding portfolio, sourcing liquidity from multiple sources depending market dynamics and interest rate movements. The funding composition remained relatively unchanged with deposits accounting for 65% of the total funding base, followed by borrowings [26%] and shareholders' funds [9%].

Funding Composition



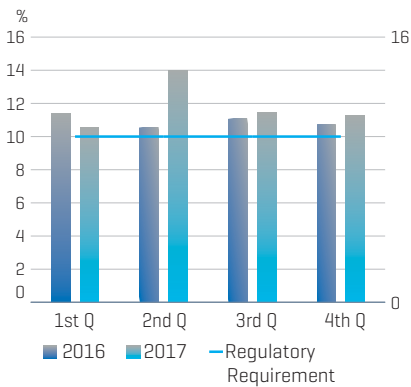
| Capital adequacy ratio | 2017 | 2016 |
|--------------------------------------|--------|--------|
| Tier 1 CAR | 10.21% | 10.66% |
| Regulatory min | 5.00% | 5.00% |
| Tier 1 CAR Industry average | 10.87% | 9.85% |
| Total capital ratio | 15.27% | 10.69% |
| Regulatory min | 10.00% | 10.00% |
| Total capital ratio Industry average | 11.5% | 10.19% |

Risk Management

Liquidity

The liquidity ratio measures the adequacy of the high -quality liquid assets maintained by the Company. During the year the Company's statutory liquidity ratio of 11.26% compared to 10.75% in 2016 and continued to be maintained above stipulated limits.

Liquid Assets Ratio



Operational risks

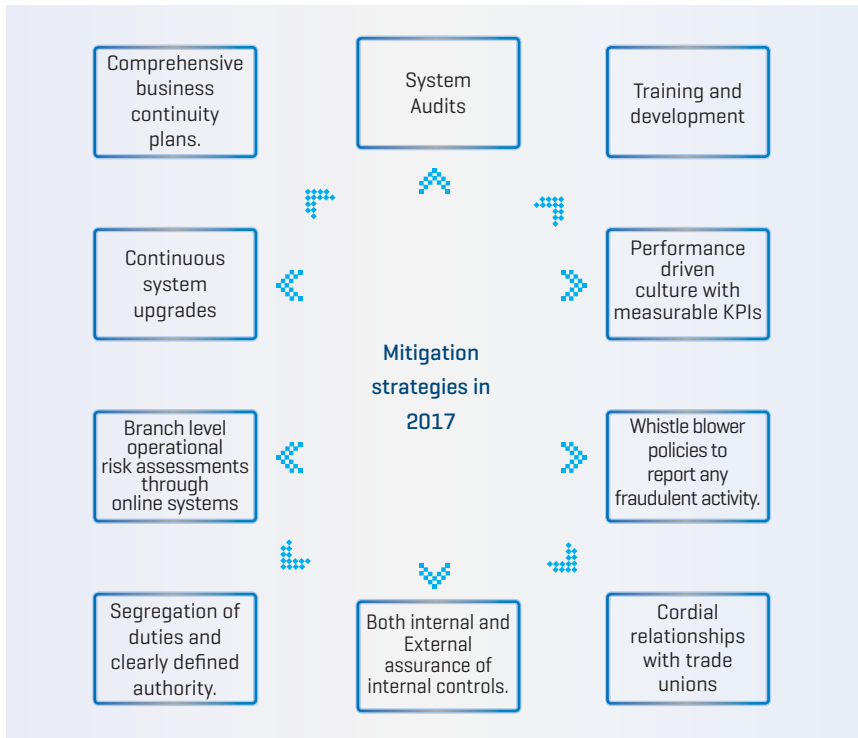
| | | |
|--|--|--|
| Losses due to inadequate/ failure of internal processors, Systems, people and external events. | Potential Impact on <ul style="list-style-type: none"> Reputation Service delivery Employee performance Resource utilization Brand image Cost and profitability | Risk mitigation <ul style="list-style-type: none"> Internal controls. Training & Development Risk aware culture. Systems inspections and business continuity plans. Well defined processors. Policies. Whistle Blowing |
|--|--|--|

Stress testing was conducted to assess the Company's ability to withstand shocks of varying gravity related to operational risk. MBSL has the ability to bear 50% level shock level while maintaining capital adequacy ratio of the company as prescribed by the CBSL.

| Description | CAR as at | | Shock Level | |
|--------------------|-----------|--------|-------------|--------|
| | 31-Dec-17 | 5% | 20% | 50% |
| Operational Risk** | | | | |
| Tier I Capital | 10.21% | 9.91% | 9.86% | 9.78% |
| Total Capital | 15.27% | 14.98% | 14.94% | 14.86% |

** Operational Loss is based on Assumption

Several risk mitigation strategies in the forms of internal controls and contingency plans are adopted throughout the Company including its widespread branch networks. Internal controls are continuously reviewed by divisional / regional managers in addition to an independent assurance of the adequacy of internal controls provided by the internal audit function.



Key focus areas in operational risk during the year under review were,

- Introduced a branch risk rating system with defined branch KPIs which are aligned to the performance management system of the branch employees
- Successful implementation of the state-of-the-art core banking system
- Ongoing training initiatives to raise risk awareness and nurture a culture of risk consciousness

Strategic Risk

| | | |
|--|---|---|
| Losses due to failure / inadequateness of strategies to meet the demands of changing operating landscapes. | <p>Potential Impact</p> <ul style="list-style-type: none"> • Profitability • Loss of customers • Cost of non-compliance to changing regulations. • Affect stakeholder relationships. • Investment • Reputation | <p>Risk mitigation</p> <ul style="list-style-type: none"> • Continuous review of economic, industry and regulatory environments. • Evaluation of competitive environments. • Stakeholder engagement. • Customer relationships. |
|--|---|---|

Business environments are continuously impacted by several variables both controllable and uncontrollable in nature. Fast changing customer preferences, changing regulations and government policies have had a significant impact on financial institutions in the recent

past that increase strategic risk. During 2017, increasing interest rates, changing loan to value ratios imposed for vehicle leasing, fast paced growth in digitalization of banking services and difficulties in credit recovery were some of the significant challenges that required an evolution in the strategy of the Company. External and internal challenges compelled the Company to revisit its medium-term strategy during the year and realign its processes to ensure sustainable and profitable business growth [refer page 54 for further information on our strategic guide agenda for the year]. Continuous stakeholder engagement through several channels acted as the means of identifying the material concerns of multiple stakeholders including shareholders, customers, employees and government.

Key aspects of MBSL's strategic risk management framework are,

- Implementation of a Board approved strategic plan which takes cognizance of industry trends, stakeholder needs and the strength and weaknesses of our value creation model
- Reviewing performance of the strategic plan against pre-defined performance indicators on a consistent basis
- Persistently monitoring industry trends including market dynamics, macro-economic changes and competitor behavior
- Conducting variance analysis by comparing budgeted against actual performance and recommending appropriate strategies.
- Conducting competitor analysis, reviewing industry trends and taking prompt actions to prevent risks.
- Conducting risk assessment prior any acquisition or investment

Risk Management

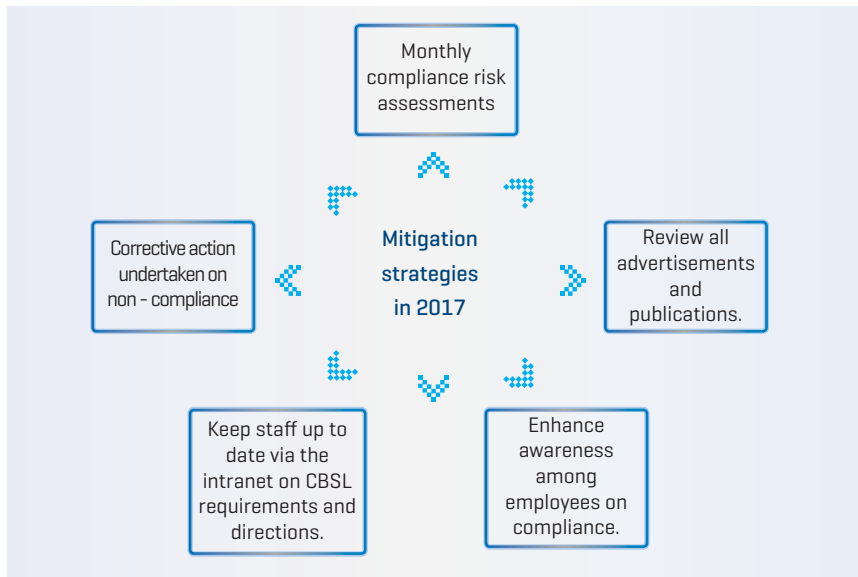
Stress Testing

| Description | CAR as at | | Shock Level | |
|--|-----------|--------|-------------|--------|
| | 31-Dec-17 | 5% | 20% | 50% |
| Strategic Risk - Investment in Insurance | | | | |
| Tier I Capital | 10.21% | 10.20% | 10.18% | 10.13% |
| Total Capital | 15.27% | 15.26% | 15.24% | 15.19% |

Compliance risks

Compliance risk is the risk arising out of non-compliance with applicable laws, regulations, codes of conduct and standards of good practice culminating in financial loss, or loss to the Company’s reputation.

MBSL’s dedicated compliance officer is responsible for monitoring the Company’s overall compliance risks. Compliance checks are conducted for all business units on a monthly basis and prompt action is taken in instances of non-compliance. The IRMC also monitors the Company’s compliance through regular reporting from the Compliance division.



Further, all the advertisements, publications are reviewed by the Compliance division to ensure that the publications are in line with relevant compliance requirements. The Company has also educated the MBSL staff regarding the compliance requirements and regulations stipulated by the CBSL directions, through training programs and the intranet in order to minimize the violations/non compliances of any such requirement by the company.

Reputation Risk

Reputational risk impacts the Company’s current or prospective earnings capacity and Organizational value arising from the loss of confidence, breakdown in relationships and negative perceptions of transactional stakeholders. The consequences of reputational risks are long lasting and could prompt a drawback of deposits, rating downgrades and additional costs. Main aspects of the Company’s reputation risk management framework are as follows;

- Strong stakeholder engagement which enabled prompt identification and response of stakeholder needs including customers, shareholders and employees.
- Compliance to all CBSL and other regulations ensuring that the Company has adequate capital buffers to meet its obligations.
- Lending rates maintained in line with CBSL guidelines.
- Implemented policies such as customer due diligence, Know Your Customer and Anti Money Laundering policies. During the year, we also further strengthened the customer due diligence process including identification of Politically Exposed Persons.

Creating value for stakeholders



FINANCIAL INFORMATION

Financial Calendar

DATE

2017

| | |
|---|---------------|
| Publication of unaudited interim Financial Statements for the quarter ended 31 December 2016 | 02-Mar-2017 |
| Authorization of issue of Financial Statements for the year ended 31 December 2016 | 28-April-2017 |
| Allotment of Debentures -2017 | 12-May-2017 |
| Publication of unaudited interim Financial Statements for the quarter ended 31 March 2017 | 16-May-2017 |
| Publication of Annual Report for the financial year ended 31 December 2016 | 30-May-2017 |
| 35 Annual General Meeting of the Company | 27-June-2017 |
| Publication of unaudited interim Financial Statements for the quarter ended 30 June 2017 | 17-Aug-2017 |
| Publication of unaudited interim Financial Statements for the quarter ended 30 September 2017 | 10-Nov-2017 |

2018

| | |
|--|---------------|
| Publication of unaudited interim Financial Statements for the quarter ended 31 December 2017 | 02-Mar-2018 |
| Authorization of issue of Financial Statements for the year ended 31 December 2017 | 27-April-2018 |
| Publication of unaudited interim Financial Statements for the quarter ended 31 March 2018 | 16-May-2018 |
| Publication of Annual Report for the financial year ended 31 December 2017 to be released On or before | 30-May-2018 |
| 36 Annual General Meeting of the Company | 26-June-2018 |
| Publication of unaudited interim Financial Statements for the quarter ending 30 June 2018 to be released on or before | 15-Aug-2018 |
| Publication of unaudited interim Financial Statements for the quarter ending 30 September 2018 to be released on or before | 15-Nov-2018 |
| Publication of unaudited interim Financial Statements for the quarter ending 31 December 2018 to be released on or before | 28-Feb-2019 |

Directors Statement on Internal Control Over Financial Reporting

The Board of Directors is pleased to present the Directors' Statement on Internal Control in line with the section 10(2) (b) of the Finance Companies Direction No. 03 of 2008 as amended by the Direction No. 06 of 2013.

Responsibility

The Board of Directors ("Board") is responsible for the adequacy and effectiveness of Merchant Bank of Sri Lanka & Finance PLC's (MBSL) system of internal controls. However, such a system is designed to manage the MBSL's key areas of risk within an acceptable risk profile, rather than eliminate the risk of failure to achieve the policies and business objectives of MBSL. Accordingly, the system of internal controls can only provide reasonable but not absolute assurance against material misstatement of management and financial information and records or against financial losses or fraud.

The Board has established an ongoing process for identifying, evaluating and managing the significant risks faced by MBSL and this process includes enhancing the system of internal controls as and when there are changes to business environment or regulatory guidelines.

The process is regularly reviewed by the Board and accords with the guidance for directors of Banks on the Directors' Statement of Internal Control issued by the Institute of Chartered Accountants of Sri Lanka. As per the said guidance, significant processes affecting significant accounts of MBSL were assessed along with the key risk areas of MBSL.

The Board is of the view that the system of internal controls in place is sound and adequate to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements for external purposes is in accordance with relevant accounting principles and regulatory requirements.

The management assists the Board in the implementation of the Board's policies and procedures on risk and control by identifying and assessing the risks faced by MBSL and in the design, operation and monitoring of suitable internal controls to mitigate and control these risks.

Key features of the process adopted in applying and reviewing the design and effectiveness of the internal control system on financial reporting

The key processes that have been established in reviewing the adequacy and integrity of the system of internal controls with respect to financial reporting include the following:

- Internal audit department established by the Board is to assist the Board to ensure that MBSL complies with policies and procedures, evaluate the effectiveness of the internal control system in place and highlights significant findings in respect of any non-compliance on an ongoing basis. Internal audits are carried out on all departments and branches, the frequency of which is determined by the level of risk assessed, to provide an independent and objective report on operational and management activities of these units and branches. The annual audit plan is reviewed and approved by the Audit Committee and the findings of the audits are submitted to the Audit Committee for review at their periodic meetings.
- The Audit Committee of the Company, review internal control issues identified by the internal audit division, external auditors, regulatory authorities and management, and evaluate the adequacy and effectiveness of the risk management and internal control systems. Further it highlights the areas that need more internal controls while suggesting improvements to existing internal controls. The minutes of the Audit Committee meetings are tabled to the Board on a periodic basis. Further details of the activities undertaken by the Audit Committee of the Company are set out in the Audit Committee Report in the Annual Report.
- Operational committees are established by the Board with appropriate empowerment to assist the Board in ensuring the effectiveness of the company's daily operations and that the company's operations are in accordance with the corporate objectives, strategies and the annual budget as well as the policies and business directions that have been approved.
- In assessing the internal control system, identified officers of the Company collated all procedures and controls that are connected with significant accounts and disclosures of the Financial Statements of company. These in turn were observed and checked by the Internal Audit department to verify the suitability of design and effectiveness of these procedures and controls on an ongoing basis.

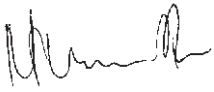
The confirmation by the Board

Based on the above processes, the Board confirms that the financial reporting system of MBSL has been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of Financial Statements for external purposes has been done in accordance with Sri Lanka Accounting Standards and regulatory requirements of the Central Bank of Sri Lanka.

Review of the statement by external auditors

Based on the procedures performed, the external auditors have reported to the Board that nothing has come to their attention that causes them to believe that this Statement is inconsistent with their understanding of the process adopted by the Board in the review of the design and effectiveness of internal control system over financial reporting of the Company.

For and on behalf of the Board,



N Perera
Director



K. B. S. Bandara
Director

17 May 2018
Colombo

Directors' Responsibility for Financial Reporting

This Statement sets out the responsibilities of the Directors in relation to the Financial Statements of the Company and the Group. The responsibilities of the auditors in relation to the financial statements are set out in the 'Independent Auditor's Report' on page 119 of the Annual Report.

In terms of Sections 150 (1), 151, 152 and 153 (1) & (2) of the Companies Act No. 07 of 2007, the Directors of the Company are responsible for ensuring that the Company and the Group keep proper books of account of all the transactions and prepare Financial Statements that give a true and fair view of the financial position of the Company and the Group as at end of each financial year and of the financial performance of the Company and the Group for each financial year and place them before a general meeting. The Financial Statements comprise of the Statement of Financial Position as at 31 December 2017, Income Statement and Other Comprehensive Income, Statement of Changes in Equity, Statement of Cash Flows for the year then ended and Notes thereto.

Accordingly, the Directors confirm that the Financial Statements of the Company and the Group give a true and fair view of:

- (a) The Financial Position of the Company and the Group as at Reporting date; and
- (b) The financial performance of the Company and the Group for the financial year ended on the reporting date.

The Directors are required to ensure that the Financial Statements of the Company and the Group for the financial year ended 31 December 2017 have been prepared and presented based on the Sri Lanka Accounting Standards [SLFRSs and LKASs], Companies Act No. 07 of 2007, Sri Lanka Accounting & Auditing standard Act No. 15 of 1995, Finance Business Act No. 42 of 2011 and Directions issued thereto, Listing Rules of the Colombo Stock Exchange, Code of Best Practice on Corporate Governance issued jointly by The Institute of Chartered Accountants of Sri Lanka [CASL] and the Securities and Exchange Commission of Sri Lanka [SEC].

The Directors have also taken reasonable measures to safeguard the assets of the Company and of the Group and to prevent and detect frauds and other irregularities. In that regard, the Directors have established appropriate systems of internal control with the view to preventing and detecting fraud and other irregularities. The Directors have reasonable expectations, after making enquiries and following a review of the Company's Budget for the ensuring year including cash flows and borrowing facilities, that the Company has adequate resources to continue in operational existence for the foreseeable future, and therefore has continued

to adopt the going concern basis in preparing the Financial Statements.

The Board of Directors also wishes to confirm that, as required by the Sections 166 (1) and 167 (1) of the Companies Act, they have prepared this Annual Report in time and ensured that a copy thereof is sent to every shareholder of the Company, who have expressed desire to receive a hard copy or to other shareholders a soft copy each in a CD containing the Annual Report within the stipulated period of time as required by the Rule No. 7.5 (a) and (b) on Continuing Listing Requirements of the Listing Rules of the Colombo Stock Exchange. The Directors also wish to confirm that all shareholders in each category have been treated equitably in accordance with the original terms of issue.

Pursuant to provision of Article 154 (4) of the Constitution of the Democratic Socialist Republic of Sri Lanka, the Auditor General is the Auditor of the Company and issue the final opinion on the Financial Statements of the Company. The responsibilities of the Auditor in relation to the Financial Statements are set out in the Report of the Auditor General on Page 119 of this Annual Report.

Compliance Report

The Directors confirm that to the best of their knowledge, all taxes, statutory levies and financial obligations of the Company and the Group have been either paid or adequately provided for in the Financial Statements. The Directors further confirm that after considering the financial position, operating conditions, regulatory and other factors and such matters required to be addressed in the 'Code on Corporate Governance' issued jointly by the Institute of Chartered Accountants of Sri Lanka and the Securities and Exchange Commission, the Directors have a reasonable expectation that the Company and the Group possess adequate resources to continue in operation for the foreseeable future. For this reason, we continue to adopt the Going Concern basis in preparing the Financial Statements. The Directors are of the view that they have discharged their responsibilities as set out in this Statement.

By Order of the Board,

K. Jayatilake

K Jayatilake
Company Secretary

17 May 2018
Colombo

Report of the Auditor General



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මගේ අංකය
எனது தீ.க. }
My No. }

BAF/B/BOC-S/MBSL/2017

ඔබේ අංකය
உமது தீ.க. }
Your No. }

දිනය
திகதி }
Date }

17 May 2018

To the Shareholders

of the Merchant Bank of Sri Lanka & Finance PLC

Report of the Auditor General on the Financial Statements of the Merchant Bank of Sri Lanka & Finance PLC and the consolidated financial statements of the company and its Subsidiary for the year ended 31 December 2017

The audit of the financial statements of the Merchant Bank of Sri Lanka & Finance PLC ["the Company"] and the consolidated financial statements of the Company and its Subsidiary ["the Group"] for the year ended 31 December 2017 comprising the statement of financial position as at 31 December 2017 and the statement of profit or loss and other comprehensive income, statement of changes in equity and the statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory information was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka. To carry out this audit I was assisted by a firm of Chartered Accountants in public practice.

Board's Responsibility for the Financial Statements

The Board of Directors ["Board"] is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the Board determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

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

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as at 31 December 2017, and of its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

Emphasis of Matter

Without qualifying my opinion, I draw your attention to the Note 44 to the financial statements which described the going concern assumption in the preparation of the financial statements of the Subsidiary, MBSL Insurance Company Limited.

Report on Other Legal and Regulatory Requirements

As required by Section 163(2) of the Companies Act No 07 of 2007, I state the following:

- [a] The basis of opinion and scope and limitations of the audit are as stated above.

Report of the Auditor General



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Auditor General's Department

(b) In my opinion:

- I have obtained all the information and explanations that were required for the audit and as far as appears from my examination, proper accounting records have been kept by the Company.
- The financial statements of the Company give a true and fair view of its financial position as at 31 December 2017, and of its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.
- The financial statements of the Company and the Group comply with the requirements of the Sections 151 and 153 of the Companies Act No. 07 of 2007.

However, it should be noted that, the net assets of the Subsidiary are less than half of the stated capital and face a serious loss of capital situation in terms of Section 220 of the Companies Act No. 07 of 2007 as discussed in Note 44 to the financial statements.

- As discussed in Note 44 to the financial statements, the Subsidiary has not segregated the long term insurance business and the general insurance business being carried on by it into two separate companies in accordance with Section 53 of Regulation of Insurance Industry (Amendment) Act No.03 of 2011.
- The non-life business of the Subsidiary does not fulfill the minimum required thresholds set for the capital adequacy ratio and total available capital by the regulation of Insurance Industry Act, No.43 of 2000, and "the Solvency Margin (Risk Based Capital) Rules 2015, while the life business does not fulfill the minimum required threshold set for total available capital.

Report to Parliament

My report to Parliament in pursuance of provisions in Article 154(6) of the Constitution will be tabled in due course.

H.M. Gamini Wijesinghe

Auditor General

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Statement of Profit or Loss

| For the year ended 31 December | | Company | | Group | |
|---|---------|-------------|-----------------|------------------------------|-----------------|
| | | Note | 2017 Rs.'000 | 2016 Rs.'000 Restated* | 2017 Rs.'000 |
| Income | 4 | 6,402,825 | 4,888,155 | 7,079,110 | 6,099,998 |
| Interest and similar income | | 6,157,286 | 4,737,774 | 6,256,612 | 4,853,007 |
| Interest and similar expenses | | (3,708,808) | (2,709,604) | (3,708,625) | (2,710,557) |
| Net interest income | 5 | 2,448,478 | 2,028,170 | 2,547,987 | 2,142,450 |
| Fee and commission income | | 179,687 | 131,483 | 140,151 | 190,723 |
| Fee and commission expenses | | (59,964) | (37,813) | (77,707) | (103,487) |
| Net fee and commission income | 6 | 119,723 | 93,670 | 62,444 | 87,236 |
| Insurance premium income | 7 | - | - | 562,170 | 995,321 |
| Net claims and benefits | | - | - | (348,999) | (845,430) |
| Net trading income | 8 | (16,018) | 10,072 | (13,769) | 5,612 |
| Net gain/(loss) on financial assets - held-for-trading | 9 | 5,624 | (61,096) | 4,771 | (58,226) |
| Other operating income | 10 | 76,246 | 69,922 | 129,175 | 113,561 |
| Total operating income | | 2,634,053 | 2,140,738 | 2,943,779 | 2,440,524 |
| Impairment charges for loans and other losses | 11 | (244,231) | (24,239) | (245,206) | (27,959) |
| Net operating income | | 2,389,822 | 2,116,499 | 2,698,573 | 2,412,565 |
| Personnel expenses | 12 | (1,027,092) | (781,530) | (1,179,659) | (993,084) |
| Retirement benefit expenses | 37.1 | (46,434) | (40,464) | (49,864) | (45,697) |
| Depreciation of property, equipment & investment properties | 26 & 27 | (82,144) | (64,408) | (95,455) | (83,487) |
| Amortisation of intangible assets | 28 | (26,881) | (10,639) | (32,731) | (18,129) |
| Other operating expenses | 13 | (743,029) | (641,940) | (923,059) | (915,175) |
| Total operating expenses | | (1,925,580) | (1,538,981) | (2,280,768) | (2,055,572) |
| Operating profit before VAT on financial services and impairment of investment in subsidiary | | 464,242 | 577,518 | 417,805 | 356,993 |
| Impairment of investment in subsidiary | | (56,189) | (232,891) | - | - |
| Profit from operations after impairment of investment in subsidiary | | 408,053 | 344,627 | 417,805 | 356,993 |
| Value Added Tax on financial services | | (179,403) | (111,730) | (179,403) | (111,730) |
| Share of associate company's profit/(loss) before tax | 24.1 | - | - | 1,059 | (5,437) |
| Profit before income tax | | 228,650 | 232,897 | 239,461 | 239,826 |
| Income tax expense | 14 | (127,799) | (154,247) | (136,112) | (165,658) |
| Profit for the year | | 100,851 | 78,650 | 103,349 | 74,168 |
| Profit for the year attributable to: | | | | | |
| Equity holders of the parent | | 100,851 | 78,650 | 111,858 | 110,879 |
| Non controlling interests | | - | - | (8,509) | (36,711) |
| Profit for the year | | 100,851 | 78,650 | 103,349 | 74,168 |
| Earnings per share: | | | | | |
| Basic/diluted earnings per share (Rs.) | 15 | 0.61 | 0.47 | 0.67 | 0.67 |

* Certain amounts shown do not correspond to the Financial Statements of 2016 as explained in note 45.

Figures in brackets indicate deductions.

The accounting policies and notes to the Financial Statements from page 128 to 227 form an integral part of the Financial Statements.

Statement of Comprehensive Income

| For the year ended 31 December | Note | Company | | Group | |
|--|------|-----------------|------------------------------|-----------------|------------------------------|
| | | 2017 Rs.'000 | 2016 Rs.'000 Restated* | 2017 Rs.'000 | 2016 Rs.'000 Restated* |
| Profit for the year | | 100,851 | 78,650 | 103,349 | 74,168 |
| Other comprehensive income/(expenses) | | | | | |
| Other comprehensive income to be re-classified to profit or loss in subsequent periods (net of tax): | | | | | |
| Gains/(Losses) on re-measuring available-for-sale financial assets | | 28,379 | [17,452] | 39,216 | [29,129] |
| Net other comprehensive income/(expenses) to be re-classified to profit or loss in subsequent periods | | 28,379 | [17,452] | 39,216 | [29,129] |
| Other comprehensive income not to be re-classified to profit or loss in subsequent periods (net of tax): | | | | | |
| Actuarial gains/(losses) on defined benefit plans | 37 | [17,867] | 39,068 | [20,448] | 40,541 |
| Share of associates company's other comprehensive income | 24.1 | - | - | 1,239 | 1,035 |
| Deferred tax effect relating to components of other comprehensive income | 14 | 15,942 | [1,810] | 15,942 | [1,810] |
| Net other comprehensive income/(expenses) not to be re-classified to profit or loss in subsequent periods | | [1,925] | 37,258 | [3,267] | 39,766 |
| Other comprehensive income/(expenses) for the year, net of tax | | 26,454 | 19,806 | 35,949 | 10,637 |
| Total comprehensive income/(expenses) for the year, net of tax | | 127,305 | 98,457 | 139,298 | 84,805 |
| Total comprehensive income/(expenses) attributable to: | | | | | |
| Equity holders of the parent | | 127,305 | 98,457 | 146,496 | 123,137 |
| Non-controlling interests | | - | - | [7,198] | [38,332] |
| Total comprehensive income/(expenses) for the year, net of tax | | 127,305 | 98,457 | 139,298 | 84,805 |

* Certain amounts shown do not correspond to the Financial Statements of 2016 as explained in note 45.

Figures in brackets indicate deductions.

The accounting policies and notes to the Financial Statements from page 128 to 227 form an integral part of the Financial Statements.

Statement of Financial Position

| As at 31 December | Note | Company | | Group | |
|--|------|-------------------|-------------------------------|-------------------|-------------------------------|
| | | 2017 Rs.'000 | 2016 Rs.'000 Restated * | 2017 Rs.'000 | 2016 Rs.'000 Restated * |
| Assets | | | | | |
| Cash and cash equivalents | 17 | 418,885 | 401,301 | 466,139 | 441,357 |
| Placements with banks & financial institutions | 18 | 1,509,597 | 118,933 | 1,597,785 | 262,319 |
| Securities purchased under resale agreements | 19.1 | 1,302,748 | 265,687 | 1,651,927 | 730,773 |
| Financial investments - held-for-trading | 20 | 231,264 | 323,655 | 238,252 | 331,586 |
| Bills receivable | 21.1 | 494,096 | 739,403 | 494,096 | 739,403 |
| Loans & advances to customers | 21.2 | 12,598,133 | 11,320,845 | 12,592,956 | 11,392,491 |
| Lease and hire purchase receivable | 21.3 | 15,661,432 | 14,991,751 | 15,661,432 | 14,991,751 |
| Financial investments - available-for-sale | 22 | 1,815,181 | 2,735,645 | 2,191,842 | 3,126,815 |
| Financial investments - held-to-maturity | 23 | 479,362 | 57,766 | 479,362 | 57,766 |
| Real estate stock | | 42,603 | 24,144 | 42,603 | 24,143 |
| Investment in associate company | 24 | 81,084 | 81,084 | 92,453 | 91,325 |
| Investment in subsidiary | 25 | 21,117 | 77,306 | - | - |
| Investment properties | 26 | 123,773 | 127,670 | 123,773 | 127,670 |
| Property and equipment | 27 | 321,660 | 316,511 | 347,393 | 358,266 |
| Intangible assets | 28 | 226,293 | 26,557 | 244,526 | 47,880 |
| Other assets | 29 | 317,979 | 318,496 | 692,427 | 891,193 |
| Total assets | | 35,645,207 | 31,926,754 | 36,916,966 | 33,614,738 |
| Liabilities | | | | | |
| Due to banks | 30 | 123,849 | 201,635 | 129,877 | 224,997 |
| Securities sold under repurchase agreements | 19.2 | 437,672 | 401,820 | 437,672 | 401,820 |
| Due to customers | 31 | 21,918,869 | 18,518,419 | 21,910,383 | 18,518,419 |
| Debt issued and borrowed funds | 32 | 8,818,862 | 8,722,787 | 8,818,862 | 8,722,787 |
| Insurance provision - life | 33.1 | - | - | 547,026 | 514,258 |
| Insurance provision - non life | 33.4 | - | - | 430,093 | 781,034 |
| Current tax liabilities | 34 | 7,473 | 151,128 | 7,473 | 141,180 |
| Deferred tax liabilities | 35 | 373,711 | 206,888 | 373,711 | 206,888 |
| Other liabilities | 36 | 467,965 | 404,174 | 719,713 | 752,034 |
| Retirement benefits obligations | 37 | 262,986 | 213,388 | 283,000 | 231,463 |
| Total liabilities | | 32,411,387 | 28,820,239 | 33,657,810 | 30,494,880 |

| As at 31 December | Note | Company | | Group | |
|--|------|-------------------|-------------------------------|-------------------|-------------------------------|
| | | 2017 Rs.'000 | 2016 Rs.'000 Restated * | 2017 Rs.'000 | 2016 Rs.'000 Restated * |
| Equity | | | | | |
| Stated capital | 38 | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 |
| Statutory reserves | 39.1 | 177,839 | 157,669 | 177,839 | 157,669 |
| Retained earnings | 39.2 | 924,947 | 846,191 | 948,415 | 859,584 |
| Available-for-sale reserve | 39.3 | 6,577 | (21,802) | 1,300 | (36,195) |
| Total equity attributable to equity holders of the parent | | 3,233,820 | 3,106,515 | 3,252,011 | 3,105,515 |
| Non-controlling interests | | - | - | 7,145 | 14,343 |
| Total equity | | 3,233,820 | 3,106,515 | 3,259,156 | 3,119,858 |
| Total liabilities and equity | | 35,645,207 | 31,926,754 | 36,916,966 | 33,614,738 |
| Commitments and contingent liabilities | 47 | 167,712 | 132,265 | 183,166 | 616,478 |
| Net Assets Value per share (Rs.) | | 19.50 | 18.73 | 19.61 | 18.72 |

* Certain amounts shown do not correspond to the Financial Statements of 2016 as explained in note 45.

Figures in brackets indicate deductions.

The accounting policies and notes to the Financial Statements from page 128 to 227 form an integral part of the Financial Statements.

These Financial Statements have been prepared in compliance with the requirements of the Companies Act No. 7 of 2007.



P. I. Kandanaarachchi
Head of Finance



D. M. N. P. Karunapala
Chief Executive Officer

The Board of Directors is responsible for the preparation and presentation of these Financial Statements.

Approved and signed for and on behalf of the Board.



Dr. S. Lokuhewa
Chairman



K. B. S. Bandara
Director

27 April 2018

Colombo, Sri Lanka

Statement of Changes in Equity

| Company | Stated | Statutory | Available-for | Retained | Total | |
|---|------------------|----------------|-----------------|----------------|------------------|--|
| | capital | reserves | -sale-reserve | earnings | equity | |
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | |
| Balance as at 01 January 2016 | 2,124,457 | 140,544 | (4,350) | 747,408 | 3,008,059 | |
| Net profit for the year | - | - | - | 78,650 | 78,650 | |
| Other comprehensive income, net of tax | - | - | (17,452) | 37,258 | 19,806 | |
| Transfers to statutory reserves | - | 17,125 | - | (17,125) | - | |
| Balance as at 31 December 2016 - Restated* | 2,124,457 | 157,669 | (21,802) | 846,191 | 3,106,515 | |
| Net profit for the year | - | - | - | 100,851 | 100,851 | |
| Other comprehensive income, net of tax | - | - | 28,379 | (1,925) | 26,454 | |
| Transfers to statutory reserves | - | 20,170 | - | (20,170) | - | |
| Balance as at 31 December 2017 | 2,124,457 | 177,839 | 6,577 | 924,947 | 3,233,820 | |

| Group | Stated | Statutory | Available-for | Retained | Non | Total |
|--|------------------|----------------|-----------------|----------------|---------------|------------------|
| | capital | reserves | -sale-reserve | earnings | controlling | Equity |
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | interests | Rs.'000 |
| Balance as at 01 January 2016 | 2,124,457 | 140,544 | (8,920) | 746,023 | 52,674 | 3,054,778 |
| Prior year adjustments | - | - | - | (19,725) | - | (19,725) |
| Balance as at 01 January 2016 after the restatement | 2,124,457 | 140,544 | (8,920) | 726,298 | 52,674 | 3,035,053 |
| Net profit for the year | - | - | - | 110,879 | (36,711) | 74,168 |
| Other comprehensive income, net of tax | - | - | (27,275) | 39,532 | (1,620) | 10,637 |
| Transfers to statutory reserves | - | 17,125 | - | (17,125) | - | - |
| Balance as at 31 December 2016 - Restated* | 2,124,457 | 157,669 | (36,195) | 859,584 | 14,343 | 3,119,858 |
| Net profit for the year | - | - | - | 111,858 | (8,509) | 103,349 |
| Other comprehensive income, net of tax | - | - | 37,495 | (2,857) | 1,311 | 35,949 |
| Transfers to statutory reserve fund | - | 20,170 | - | (20,170) | - | - |
| Balance as at 31 December 2017 | 2,124,457 | 177,839 | 1,300 | 948,415 | 7,145 | 3,259,156 |

* Certain amounts shown do not correspond to the Financial Statements of 2016 as explained in note 45.

Figures in brackets indicate deductions.

The accounting policies and notes to the Financial Statements from page 128 to 227 form an integral part of the Financial Statements.

Statement of Cash Flows

Accounting Policy

The Statement of Cash Flows has been prepared by using the 'Indirect Method' of preparing cash flow in accordance with the Sri Lanka Accounting Standard-LKAS 7-'Statement of Cash Flows', whereby operating activities, investing activities and financing activities are separately recognised. Cash and cash equivalents comprise of short-term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents as referred to in the Statement of Cash Flows is comprised of those items as explained in note 40 on page 195.

| For the year ended 31 December | Note | Company | | Group | |
|---|------|-----------------|-------------------------------|-----------------|-------------------------------|
| | | 2017 Rs.'000 | 2016 Rs.'000 Restated * | 2017 Rs.'000 | 2016 Rs.'000 Restated * |
| Cash flows from operating activities | | | | | |
| Profit before income tax | | 228,650 | 232,897 | 239,461 | 239,826 |
| Adjustments for : | | | | | |
| Change in operating assets | 40.2 | (2,041,934) | (3,899,100) | (1,765,033) | (3,990,091) |
| Change in operating liabilities | 40.3 | 3,464,241 | 2,719,447 | 3,041,470 | 2,806,239 |
| Share of associate company's profit/[loss] before tax | | - | - | (1,059) | 5,437 |
| Contribution to defined benefit plans | | 46,434 | 40,464 | 49,864 | 45,697 |
| Other non-cash items included in profit before tax | 40.4 | 382,542 | 216,994 | 345,191 | 13,175 |
| Dividends received | | (8,278) | (12,853) | (9,440) | (13,127) |
| | | 2,071,655 | (702,151) | 1,900,454 | (892,844) |
| Gratuity paid | | (14,703) | (33,539) | (20,014) | (35,733) |
| Net cash generated from/(used in) operating activities before income tax | | 2,056,952 | (735,690) | 1,880,440 | (928,577) |
| Tax paid | | (10,590) | (57,994) | (10,590) | (69,683) |
| Net cash generated from/(used in) operating activities | | 2,046,362 | (793,684) | 1,869,850 | (998,260) |
| Cash flows from investing activities | | | | | |
| Purchase of financial assets designated at FVPL | | (66,490) | (31,279) | (66,400) | (33,716) |
| Proceeds from disposal of financial assets designated at FVPL | | 140,209 | 185,713 | 141,296 | 189,128 |
| Purchase of financial investments-AFS & HTM | | (610,846) | (3,082,222) | (584,261) | (3,243,384) |
| Net proceeds from sale of financial investments-AFS & HTM | | 1,180,014 | 2,228,223 | 1,180,014 | 2,228,223 |
| Net increase/(decrease) in other investment | | (1,390,664) | 321,160 | (1,335,466) | 309,353 |
| Purchase of property & equipment | | (82,538) | (159,247) | (82,689) | (160,095) |
| Purchase of intangible assets | | (226,617) | - | (229,377) | (2,385) |
| Proceeds from sale of property & equipment | | 2,796 | 50,291 | 6,722 | 51,649 |
| Dividend received | | 8,278 | 12,853 | 9,440 | 13,127 |
| Net cash used in investing activities | | (1,045,858) | (474,508) | (960,721) | (648,100) |
| Cash flows from financing activities | | | | | |
| Net increase/(decrease) reverse repo and repo agreements | | (1,001,209) | 505,626 | (885,302) | 864,277 |
| Net increase/(decrease) in other borrowings | | 1,466,798 | 1,173,945 | 1,466,798 | 1,173,945 |
| Payments on redemption of debentures | | (1,370,723) | (334,481) | (1,370,723) | (334,481) |
| Net cash used in financing activities | | (905,134) | 1,345,090 | (789,227) | 1,703,741 |
| Net decrease in cash and cash equivalents during the year | | 95,370 | 76,898 | 119,902 | 57,381 |
| Cash and cash equivalents at the beginning of year | | 199,666 | 122,768 | 216,360 | 158,979 |
| Cash and cash equivalents at the end of year | | 295,036 | 199,666 | 336,262 | 216,360 |
| Analysis of cash and cash equivalents, at the end of the year | | | | | |
| | 40.1 | | | | |
| Cash and short-term funds | | 418,885 | 401,301 | 466,139 | 441,357 |
| Due to banks | | (123,849) | (201,635) | (129,877) | (224,997) |
| | | 295,036 | 199,666 | 336,262 | 216,360 |

Figures in brackets indicate deductions.

The accounting policies and notes to the Financial Statements from page 128 to 227 form an integral part of the Financial Statements.

Notes to the Financial Statements

Section 01

Corporate Information

This section gives a description of the reporting entity, the principal activities of the Company and Group entity and the identification of Financial Statements and their authorization.

1.1 Reporting Entity

Merchant Bank of Sri Lanka & Finance PLC (MBSL) is a public quoted company incorporated in 1982 and domiciled in Sri Lanka. It is registered under the provisions of the Finance Business Act No.42 of 2011. The ordinary shares of the Company are listed in the Colombo Stock Exchange. The Company was re-registered under the Companies Act No.07 of 2007. The Company changed its name as Merchant Bank of Sri Lanka & Finance PLC with effect from November 21, 2014 and it was formerly known as Merchant Bank of Sri Lanka PLC. MBSL Savings Bank Limited and MCSL Financial Services Limited were amalgamated with Merchant Bank of Sri Lanka & Finance PLC on 01 January 2015. Consequent to the amalgamation Merchant Bank of Sri Lanka & Finance PLC remains as the surviving entity. The registered office of the Company is located at the Bank of Ceylon Merchant Tower, No. 28, St Michael's Road, Colombo 03

1.2 Consolidated Financial Statements

The Consolidated Financial Statements of Merchant Bank of Sri Lanka & Finance PLC for the year ended 31 December 2017, comprise the Company and its subsidiary (together referred to as the 'Group'), and the Group's interest in its associate company.

Parent Entity & Ultimate Parent Entity

In the opinion of the Directors, the Company's parent entity and its ultimate parent entity is Bank of Ceylon.

Number of Employees

The staff strength of the Company and the Group as at 31 December 2017 were 968 and 1,246 respectively. (917 and 1,423 as at 31 December 2016)

1.3 Group Information

Principal Activities and Nature of Operations

| Entity | Principle Business Activities |
|--|---|
| Company | |
| Merchant Bank of Sri Lanka & Finance PLC | Leasing, hire purchase, corporate and retail credit, corporate advisory services, capital market operations, margin trading, micro financing, agricultural credit facilities, real estate, pawning operations, islamic finance and accepting of savings and fixed deposits. |
| Subsidiary | |
| MBSL Insurance Company Limited | Underwriting of all classes of life and general insurance |
| Associate | |
| Lanka Securities (Pvt) Limited | Registered stock broker which engages in equity trading, debt trading and margin trading |

There were no significant changes in the nature of the principal activities of the Company and the Group during the financial year under review.

1.4 Approval of Financial Statements by the Board of Directors

The Financial Statements of the Company and the Group for the year ended 31 December 2017 (including comparatives) were approved and authorised for issue on 27 April 2018 in accordance with the resolution of the Board of Directors on 27 April 2018.

Section 02

Basis of Preparation

This section provides the basis of preparation and presentation of Financial Statements including significant accounting policies and application of Sri Lanka Accounting Standards and other related statutory requirements.

2.1 Basis of Preparation and Other Significant Accounting Policies

Summary of significant accounting policies, significant accounting judgements, estimates and assumptions used, other general accounting policies and Sri Lanka Financial Reporting Standards (SLFRS) not yet adopted are provided in this section.

All specific accounting policies and accounting estimates in relation to the reported values have been presented in the respective notes.

2.2 Statement of Compliance

The consolidated Financial Statements of the Group and separate financial statements of the Company, as at 31 December 2017 and for the year ended, have been prepared and presented in accordance with Sri Lanka Financial Reporting Standards (SLFRS and LKAS), laid down by the Institute of Chartered Accountants of Sri Lanka and in compliance with the requirements of the Companies Act No. 07 of 2007, the Finance Business Act No.42 of 2011, Regulation of Insurance Industry Act No.43 of 2000 and the Listing Rules of the Colombo Stock Exchange.

These Financial Statements include the following components:

- Statement of Profit or Loss and Statement of Comprehensive Income providing the information on the financial performance of the Company and the Group for the year under review [Refer pages 122 to 123];
- A Statement of Financial Position providing the information on the financial position of the Company and the Group as at year end [Refer page 124];
- A Statement of Changes in Equity depicting all changes in shareholders' equity during the year under review of the Company and the Group [Refer page 126];
- A Statement of Cash Flows providing the information to the users, on the ability of the Company and the Group to generate cash and cash equivalents and the needs of entity to utilise those cash flows [Refer page 127]; and
- Notes to the Financial Statements comprise accounting policies and other explanatory information [Refer pages 128 to 227].

2.3 Responsibility for Financial Statements

The Board of Directors is responsible for the preparation and presentation of these Financial Statements of the Company and the Group as per the provision of the Companies Act No. 07 of 2007 and SLFRS and LKAS.

The Board of Directors acknowledges their responsibility in relation to the Financial Statements, as set out in the 'Statement of Directors' Responsibility for Financial Reporting', 'Annual Report of the Board of Directors on the Affairs of the Company' and in the certification on the Statement of Financial Position on pages 124 to 125 respectively.

2.4 Basis of Measurement

The Financial Statements of the Company and the Group have been prepared on accrual basis under historical cost convention and applied consistently with no adjustment being made for inflationary factors affecting the Financial Statements except for the following material items in the Statement of Financial Position and Statement of Comprehensive Income.

| Item | Basis of measurement | Note no./s | Page reference |
|-------------------------------------|---|------------|----------------|
| Available-for-sale financial assets | Fair value | 22 | 168 |
| Financial assets held-for-trading | Fair value | 20 | 153 |
| | Liability for defined benefit obligations is recognised as the present value of the defined benefit obligation, plus unrecognised actuarial gains, less unrecognised past service cost and unrecognised actuarial losses. | 37 | 193 |

2.5 Functional and Presentation Currency

The Financial Statements of the Company and the Group are presented in Sri Lanka Rupees, which is the Group's functional and presentation currency.

2.6 Presentation of Financial Statements

The assets and liabilities of the Company and the Group in the Statement of Financial Position are grouped by nature and listed in an order that reflects their relative liquidity and maturity pattern. The accounting principles are applied consistently other than where specially disclosed with due regard to prudence, materiality and substance over form criteria as explained in Sri Lanka Accounting Standards-LKAS 01-'Presentation of Financial Statements'. Where appropriate, the accounting policies are disclosed in the succeeding notes.

Notes to the Financial Statements

2.7 Use of Materiality, Offsetting and Rounding

Materiality & Aggregation

Each material class of similar items is presented separately in the Financial Statements. Items of dissimilar nature or function are presented separately unless they are immaterial as permitted by the Sri Lanka Accounting Standard-LKAS 01-‘Presentation of Financial Statements’.

Offsetting

Assets and liabilities and income and expenses in the Financial Statements are not set off unless required or permitted by Sri Lanka Accounting Standards.

Rounding

The amounts in the Financial Statements have been rounded off to the nearest Rupees thousand,(Rs.'000) except where otherwise indicated.

2.8 Summary of Significant Accounting Judgments, Estimates and Assumptions

The preparation of the Financial Statements of the Company and the Group in conformity with SLFRSs/ LKASs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses and disclosure of contingencies. Judgments and estimates are based on historical experience and other factors, including expectations that are believed to be reasonable under the circumstances. Hence, actual experience and results may differ from these judgments and estimates. Estimates and underlying assumptions are reviewed on an ongoing basis and revisions to accounting estimates are recognised prospectively.

Information about significant areas of estimation, uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the Financial Statements are described in the relevant notes as follows.

- Impairment losses on non-financial assets - Note No. 25, 26, 27 & 28
- Deferred tax liabilities - Note No. 35
- Provision for impairment of loans and advances - Note No. 21
- Retirement benefits obligation - Note No.37
- Provision and contingent liabilities - Note No. 47

2.8.1 Going Concern

The management has made an assessment of the Company’s ability to continue as a going concern and is satisfied that the Company has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Company’s ability to continue as a going concern. Therefore, the Financial Statements continue to be prepared on the going concern basis.

2.8.2 Events After the Reporting Period

Events after the reporting period are those events, favorable and unfavorable, that occur between the reporting date and the date when the Financial Statements are authorized for issue.

In this regard, all material and important events that occurred after the reporting period have been considered and appropriate adjustments are made where necessary. Information on events after the reporting period are disclosed under Note No. 43 on page 201.

Section 03

3 Significant Accounting Policies

3.1 Basis of Consolidation

The Consolidated Financial Statements for the year ended 31 December 2017 comprise the Financial Statements of the Company (Parent Company) and its subsidiary (together referred to as the “Group”) and the Company’s interest in associate company. The Financial Statements of all companies in the Group have common financial year which ends on 31 December, and use consistent accounting policies.

Intra-group balances and transactions, income and expenses and any unrealised gains arising from intra-group transactions are eliminated in preparing the Consolidated Financial Statements.

3.2 Business Combination & Goodwill

Business combinations are accounted for using the acquisition method as per requirements of

Sri Lanka Financial Reporting Standard-SLFRS 03-‘Business Combinations’.

The Group measures goodwill as the fair value of the consideration transferred including the recognised amount

of any non-controlling interest in the acquiree, less the net recognised amount of the identifiable assets acquired and liabilities assumed, all measured as of the acquisition date. When the excess is negative, a bargain purchase gain is recognised immediately in the Statement of Profit or Loss.

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net amount of the identifiable assets, liabilities and contingent liabilities acquired.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually, or more frequently, if events or changes in circumstances indicate that the carrying value may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's Cash Generating Units (CGUs) or group of CGUs, which are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill forms part of a CGU (or group of CGUs) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in these circumstances is measured based on the relative values of the operation disposed of and the portion of the CGU retained.

3.3 Common Control Business Combination

Common control business combinations are accounted using the guidelines issued under Statement of Recommended Practice (SoRP) - Merger accounting for common control business combination issued by the Institute of Chartered Accountants of Sri Lanka.

Accordingly,

- The net assets of the combining entities are consolidated using the existing book values.
- No amount is recognised as goodwill which arises as a result of difference between the consideration and net assets acquired.
- Comparative amounts in the Financial Statements are restated as if the companies had been combined at the previous reporting date.

3.3.1 Loss of Control

Upon the loss of control, the Group de-recognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in the Statement of Profit or Loss. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that the control is lost. Subsequently it is accounted for as equity accounted investee or in accordance with the Group's accounting policy for financial instruments depending on the level of influence retained.

3.3.2 Transactions Eliminated on Consolidations

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated Financial Statements. Unrealized gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

3.4 Foreign Currency

3.4.1 Foreign Currency Transactions and Balances

All foreign exchange transactions are converted to functional currency which is Sri Lankan Rupees (Rs.), at the rates of exchange prevailing at the time the transactions are effected.

Monetary assets and liabilities denominated in foreign currency are retranslated to the functional currency equivalents at the spot exchange rate prevailing at the reporting date.

The gains or losses arising on translation of monetary items are recognised in the Statement of Profit or Loss.

3.5 Financial Instruments

3.5.1 Date of Recognition

Financial assets and financial liabilities are initially recognised when a group entity becomes a party to the contractual provisions of the instruments. All regular way purchases or sales of financial assets are recognised and de-recognised on a trade date basis. Regular way purchases or sales are the purchases or sales of financial

Notes to the Financial Statements

assets that require delivery of assets within the time frame established by regulation or convention in the market place.

3.5.2 Initial Measurement of Financial Instruments

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

3.5.3 Classification & Subsequent Measurement of Financial Assets

At the inception, financial assets are classified in to one of the following categories:

- Fair value through profit or loss (FVTPL) (either as held-for-trading or designated at fair value through profit or loss)
- Loans and receivables (L & R)
- Held-to-maturity financial assets (HTM)
- Available-for-sale financial assets (AFS)

The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

3.5.4 Effective Interest Method (EIR)

The effective interest method is a method of calculating the amortised cost of a financial instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Income is recognised on an effective interest basis for financial instruments other than those financial assets classified as at FVTPL.

3.5.5 Financial Assets and Liabilities Measured at Fair Value Through Profit or Loss

a) Financial Assets Held-for-Trading

Financial assets are classified as held-for-trading if they are acquired principally for the purpose of selling or repurchasing in the near term or holds as a part of a portfolio that is managed together for short-term profit or position taking.

Financial assets held-for-trading are recorded in the Statement of Financial Position at fair value. Changes in fair value are recognised in statement of profit or loss, Interest and dividend income is recorded in 'Net trading income' according to the terms of the contract, or when the right to receive the payment has been established. The Group evaluates its financial assets held for trading, other than derivatives, to determine whether the intention to sell them in the near-term is still appropriate. When the Group is unable to trade these financial assets due to inactive markets and management's intention to sell them in the foreseeable future significantly changes, the Group may elect to re-classify these financial assets in rare circumstances. Financial assets held-for-trading include instruments such as government and other debt securities and equity instrument that have been acquired principally for the purpose of selling or re-purchasing in the near term and derivatives, including separated embedded derivatives explained below unless they are designated as effective hedging instruments.

b) Financial Assets and Liabilities Designated at Fair Value Through Profit or Loss

Financial assets and financial liabilities classified in this category are those that have been designated by the management on initial recognition. Management may only designate an instrument at fair value through profit or loss upon initial recognition when the following criteria are met, and designation is determined on an instrument by instrument basis.

- The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognizing gains or losses on them on a different basis.
- The assets and liabilities are part of a group of financial assets, financial liabilities or both which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.

Financial assets and financial liabilities at fair value through profit or loss are recorded in the statement of financial position at fair value. Changes in fair value are recorded in 'Net gain or loss on financial assets designated at fair value through profit or loss'. Interest earned is accrued in 'Interest income', using the effective interest rate (EIR), while dividend income is recorded in 'Net trading income' when the right to the payment has been established.

3.5.6 Financial Liabilities at Amortised Cost

Financial instruments issued by the Company and the Group that are not designated at fair value through profit or loss, are classified as financial liabilities at amortised cost.

After the initial recognition, these financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis. The effective interest method as a method of calculating the amortised cost of a financial liability and allocating interest expense over the relevant period.

3.5.7 De-recognition of Financial Assets and Financial Liabilities

3.5.7.1 Financial Assets

A financial asset [or, where applicable a part of a financial asset or part of a group of similar financial assets] is de-recognised when:

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

On de-recognition of a financial asset, the difference between the carrying amount of the asset [or the carrying amount allocated to the portion of the asset transferred], and consideration received [including any

new asset obtained less any new liability assumed] and any cumulative gain or loss that had been recognised in Other Comprehensive Income is recognised in Statement of Profit or Loss.

When the Company and the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all of the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Company's and the Group's continuing involvement in the asset. In that case, the Company and the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Company and the Group has retained.

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

3.5.7.2 Financial Liabilities

A financial liability is de-recognised when the obligation under the liability is discharged or cancelled or expired. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in statement of profit or loss.

3.5.8 Offsetting of Financial Instruments

Financial assets and financial liabilities are offset and the net amount reported in the Consolidated Statement of Financial Position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Income and expenses are presented on a net basis only when permitted under SLFRSs, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

Notes to the Financial Statements

3.5.9 Determination of Fair Value

The fair value for financial instruments traded in active markets at the statement of financial position date is based on their quoted market price without any deduction for transaction costs.

For all other financial instruments not traded in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include the discounted cash flow method, comparison to similar instruments for which market observable prices exist and other relevant valuation models.

Certain financial instruments are recorded at fair value using valuation techniques in which current market transactions or observable market data are not available. Their fair value is determined using valuation models with the group's best estimate of the most appropriate model assumptions.

3.6 Impairment of Non-Financial Assets

The Group assesses at each reporting date to ascertain whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or Cash Generating Units (CGU) fair value less costs to sell and its value in use. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered as impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If no such transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples or other available fair value indicators.

Impairment losses are recognised immediately in statement of profit or loss. For assets excluding goodwill, an assessment is made at each reporting date to determine as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the

group estimates the asset's or CGU's recoverable amount. Previously recognised impairment losses are reversed only if there has been a change in the assumptions used to determine the recoverable amount of the asset since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the Statement of Profit or Loss.

3.7 Provisions

A provision is recognised in the Statement of Financial Position when the Group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation and the amount of the provision can be measured reliably in accordance with the Sri Lanka Accounting Standard-LKAS 37-'Provisions, Contingent Liabilities and Contingent Assets'. The amount recognised is the best estimate of the consideration required to settle the present obligation at the Reporting date, taking into account the risks and uncertainties surrounding the obligation at that date. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is determined based on the present value of those cash flows.

3.8 Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset that normally 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 the assets are substantially ready for their intended use or sale. Income earned from temporarily investing specific borrowings pending their expenditure on a qualifying asset is deducted from the borrowing costs eligible to be added to the carrying amount. All other borrowing costs are recognised in the statement of profit or loss in the period in which they are incurred in accordance with Sri Lanka Accounting Standard LKAS 23 - 'Borrowing cost'. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

3.9 Significant Accounting Policies that are Specific to the Business of the Subsidiary – MBSL Insurance Company Limited

3.9.1 Deferred Expenses

3.9.1.1 Deferred Acquisition Costs (DAC)

The costs of acquiring new businesses including commission, underwriting, marketing and policy issue expenses, which vary with and directly related to production of new businesses and/or investment contracts with Discretionary Participation Feature (DPF), are deferred to the extent that these costs are recoverable out of future premiums. All other acquisition costs are recognised as an expense when incurred. Subsequent to initial recognition, DAC for general insurance is amortised over the period on the basis Unearned Premium is amortised. The reinsurances' share of deferred acquisition cost is amortised in the same manner as the underlying asset amortisation is recorded in the statement of comprehensive income.

Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period and are treated as a change in an accounting estimate.

DAC are de-recognised when the related contracts are either expired or cancelled.

3.9.1.2 Reinsurance Commissions

Commissions receivable on outwards reinsurance contracts are deferred and amortised.

3.9.2 Reinsurance

The subsidiary-MBSL Insurance (MBSLI) cedes insurance risk in the normal course of business for all of its businesses. Reinsurance assets represent balances due from reinsurance companies. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision or settled claims associated with the reinsurer's policies and are in accordance with the related reinsurance contract.

Reinsurance assets are reviewed for impairment at each reporting date or more frequently when an indication of impairment arises during the reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that the Subsidiary-MBSLI may not receive all outstanding amounts due under the terms

of the contract and the event has a reliably measurable impact on the amounts that the company will receive from the reinsurer. The impairment loss is recorded in the statement of comprehensive income.

The Subsidiary-MBSLI also assumes reinsurance risk in the normal course of business for life insurance and non-life insurance contracts where applicable. Premiums and claims on assumed reinsurance are recognised as revenue or expenses in the same manner as they would be if the reinsurance were considered direct business, taking into account the product classification of the reinsured business. Reinsurance liabilities represent balances due to reinsurance companies. Amounts payable are estimated in a manner consistent with the related reinsurance contract.

Premiums and claims are presented on a gross basis for both ceded and assumed reinsurance.

Reinsurance assets or liabilities are de-recognised when the contractual rights are extinguished or expire or when the contract is transferred to another party.

3.9.3 Insurance Contract Liabilities

3.9.3.1 Life Insurance Contract Liabilities

Life insurance liabilities are recognised when contracts are entered into and premiums are received. These Liabilities are measured by using the net premium method. The liability is determined as the sum of the discounted value of the expected future benefits, claims handling and policy administration expenses, policyholder options and guarantees and investment income from assets backing such liabilities, which are directly related to the contract, less the discounted value of the expected theoretical premiums that would be required to meet the future cash outflows based on the valuation assumptions used. The liability is either based on current assumptions or calculated using the assumptions established at the time the contract was issued, in which case a margin for risk and adverse deviation is generally included. A separate reserve for longevity may be established and included in the measurement of the liability. Furthermore, the liability for life insurance contracts comprises the provision for unearned premiums and unexpired risks, as well as for claims outstanding, which includes an estimate of the incurred claims that have not yet been reported to the company. Adjustments to the liabilities at each reporting date are recorded in the statement of comprehensive income. Profits originated from margins of adverse deviations on run-off contracts are recognised in the

Notes to the Financial Statements

Statement of Profit or Loss over the life of the contract, whereas losses are fully recognised in the Statement of Comprehensive Income during the first year of run-off. The liability is derecognised when the contract expires, is discharged or is cancelled.

Liability Adequacy Test (LAT)

At each reporting date, an assessment is made to ascertain whether the recognised life insurance liabilities are adequate, net of related PVIF and DAC, by using an existing liability adequacy test. The Liability value is adjusted to the extent that it is insufficient to meet future benefits and expenses. In performing the adequacy test, current best estimates of future contractual cash flows, including related cash flows such as claims handling and policy administration expenses, policyholder options and guarantees, as well as investment income from assets backing such liabilities, are used. A number of valuation methods are applied, including discounted cash flows, option pricing models and stochastic modeling, to the extent that the test involves discounting of cash flows, the interest rate applied may be based on management's prudent expectation of current market interest rates. Any inadequacy is recorded in the Statement of Profit or Loss, initially by impairing PVIF and DAC and, subsequently, by establishing a technical reserve for the remaining loss. In subsequent periods, the liability for a block of business that has failed the adequacy test is based on the assumptions that are established at the time of the loss recognition. The assumptions do not include a margin for adverse deviation.

3.9.3.2 Non-Life Insurance Contract Liabilities

Non-life insurance contract liabilities are recognised when contracts are entered into and premiums are charged. These liabilities are known as the outstanding claims provision, which are based on the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related claims handling costs and reduction for the expected value of salvage and other recoveries. Delays can be experienced in the notification and settlement of certain types of claims, therefore the ultimate cost of these cannot be known with certainty at the reporting date. The liability is calculated at the reporting date using a range of standard actuarial claim projection techniques, based on empirical data and current assumptions that may include a margin for adverse deviation. The liability is not discounted for the time value of money. No provision for equalisation or catastrophe reserves is recognised. The liabilities are de-

recognised when the contract expires, is discharged or is cancelled.

Liability Adequacy Test (LAT)

The provision for unearned premiums represents premiums received for risks that have not yet expired. Generally the reserve is released over the term of the contract and is recognised as premium income. At each reporting date the company reviews its unexpired risk and a liability adequacy test is performed to determine whether there is any overall excess of expected claims and deferred acquisition costs over unearned premiums. This calculation uses current estimates of future contractual cash flows after taking account of the investment return expected to arise on assets relating to the relevant non-life insurance technical provisions. If these estimates show that the carrying amount of the unearned premiums (less related deferred acquisition costs) is inadequate, the deficiency is recognised in the Statement of Profit or Loss by setting up a provision for liability adequacy.

3.9.3.3 Investment Contract Liabilities

Investment contracts are classified between contracts with and without Discretionary Participation Feature (DPF). The accounting policies for investment contract liabilities with DPF are same as those for life insurance contract liabilities.

Investment contract liabilities without DPF are recognised when contracts are entered into and premiums are charged. These liabilities are initially recognised at fair value this being the transaction price excluding any transaction costs directly attributable to the issue of the contract. Subsequent to initial recognition investment contract liabilities are measured at fair value through profit or loss.

Deposits and withdrawals are recorded directly as an adjustment to the liability in the Statement of Financial Position. Fair value adjustments are performed at each reporting date and are recognised in the Statement of Profit or Loss. Fair value is determined through the use of prospective discounted cash flow techniques. For unitised contracts, fair value is calculated as the number of units allocated to the policyholder in each unit-linked fund multiplied by the unit-price of those funds at the statement of reporting date. The fund assets and fund liabilities used to determine the unit-prices at the reporting date are valued on a basis consistent with their

measurement basis in statement of financial position adjusted to take account of the effect on the liabilities of the deferred tax on unrealized gains on assets in the fund.

Non-unitised contracts are subsequently also carried at fair value, which is determined by using valuation techniques such as discounted cash flows and stochastic modeling. Models are validated, calibrated and periodically reviewed by an independent qualified person.

The liability is de-recognised when the contract expires, is discharged or is cancelled. For a contract that can be cancelled by the policyholder, the fair value cannot be less than the surrender value.

When contracts contain both a financial risk component and a significant insurance risk component and the cash flows from the two components are distinct while they can be measured reliably, the underlying amounts are unbundled. Any premiums relating to the insurance risk component are accounted for on the same bases as insurance.

3.9.4 Discretionary Participation Features (DPF)

A DPF is a contractual right that gives holders of these contracts the right to receive as a supplement to guaranteed benefits, significant additional benefits which are based on the performance of the assets held within the DPF portfolio. Under the terms of the contracts surpluses in the DPF funds can be distributed to policyholders and shareholders on a 90/10 basis. The Group has the discretion over the amount and timing of the distribution of these surpluses to policyholders. All DPF liabilities including unallocated surpluses, both guaranteed and discretionary, at annually are held within insurance or investment contract liabilities as appropriate.

3.10 New Accounting Standards Issued but not yet Effective

The following new accounting standards and amendments/improvements to existing standards which have been issued by the Institute of Chartered Accountants of Sri Lanka (CASL) are not effective as at 31 December 2017. None of these have been early adopted by the Company and the Group.

3.10.1 SLFRS 9 Financial Instruments

SLFRS 9, issued in 2014, replaces the existing guidance in LKAS 39- 'Financial Instruments: Recognition and Measurement' which is effective for Annual periods on or after 1 January 2018.

The initial assessment and analysis stage was completed for impairment in 2017, and the Finance team is finalising the classification and measurement phase.

Company performed the Diagnostic Phase (Preliminary Impact Assessment exercise) and Implementation Phase (solution development) on SLFRS 09- 'Financial Instruments'. The company has undertaken a significant analysis of how SLFRS 9 should be implemented and has taken tentative accounting policy decisions.

Classification & Measurement

From a classification and measurement perspective, the new standard will require all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics.

Business Model Assessment

The Company and the Group determines its business model at the level that best reflects how it manages the financial assets to achieve its objectives. The Company and the Group's business model is not assessed on an instrument by instrument basis, but at a higher level of aggregated portfolios and is based on observable factors such as :

- How the performance of the business model and the financial asset held within that business model are evaluated and reported to the Group's key management personnel.
- The risks that affects the performance of the business model (and the financial asset held within that business model) and, in particular, the way those are managed.
- How managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cashflow collected).
- The expected frequency, value and timing of sales are also important aspect of the Company and the Group assessment.

The business model assessment is based on reasonably expected scenarios without taking 'Worst case' or 'Stress

Notes to the Financial Statements

Case' scenarios in to account. If cashflows after initial recognition are realized in away that is different from the Company and the Group original expectation, the Company and the Group does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased Financial Assets

Contractual Cash Flow Characteristic Test

As the second test of the classification process the Company and the Group assesses the contractual terms of the financial asset to identify whether they meet Solely the Payment of Principal & Interest [SPPI].

Principal for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset [for example, if there are repayments of principal or amortisation of the premium/discount].

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make SPPI assessment, the Company and the Group applies judgment and considers relevant factors such as currency in which the financial asset is denominated and the period for which the interest rate is set.

In contrast to contractual exposures that introduce a more than de minimis exposure to risk or volatility in the contractual cashflows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely the payment of principle and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL

Impairment of Financial Assets

Overview of Expected Credit Loss Principle [ECL]

SLFRS 9 will principally change the Company's loan loss provision method by replacing LKAS 39-'Financial Instrument Recognition & Measurement's' incurred loss approach with a forward looking ECL Approach.

ECL allowance will be based on credit losses expected to arise over the life of the asset [Lifetime expected credit loss or LTECL], unless there has been no significant increase in credit risk since origination in which case, the loss allowance will be 12 month expected credit loss [12mECL]

12mECL is the portion of LTECL that represent the ECL that results from default events on a financial instrument that are possible within 12 months.

The Company has established a policy to perform an assessment, at the end of each reporting period of whether a financial instrument's credit risk has increased significantly since initial recognition. Based on such process the Company groups loans in to stage 1, stage 2, stage 3 as described below :

- Stage 1 : When loans are first recognised, the Company recognises an allowance based on 12mECL. Stage 1 loans also include the facilities where the credit risk has improved and the loans has been re-classified from Stage 2. Assessment of Stage 1 will be performed collectively.
- Stage 2 : When a loan has shown a significant increase in credit risk since origination, the Company records an allowance for the LTECL. Stage 2 loans also include facilities, where the credit risk has improved and the loan has been reclassified from stage 2. Assessment of stage 2 will be performed collectively.
- Stage 3 : Loan considered to be credit Impaired/ contains objective evidence of incurred losses records an allowance for the LTECL. Stage 3 assessment will be performed Individually/Collectively.

Significant Increase in Credit Risk

The Company continuously monitors all assets subject to ECL, in order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Company assess to ascertain whether there has been a significant increase in credit risk since initial recognition. The Company considers an exposure to have significantly increased in credit risk when either of the following criterias are met :

- Facilities exceeding 30 days past due.
- Counterparties/facilities reflected coded any elevated risk industries as per the assessment performed by the Credit Risk Management Team.
- Re-structured facilities.
- Secondary qualitative indicators triggering a

significant increase in credit risk for an asset, such as moving a customer/facility to watchlist.

Individually Significant Assessment and Not Impaired Individually

Individual assessment will be performed for all the customers with Objective evidence of incurred losses [under Stage 3]. Loans which are individually significant but not impaired will be assessed collectively for impairment either under Stage 1 or Stage 2 based on the criteria whether there have been significant credit deterioration since origination.

Objective evidence of incurred losses [under Stage 3]. Loans which are individually significant but not impaired will be assessed collectively for

While establishing significant credit deterioration Company will consider the following criterias :

- Other changes in the rates or terms of an existing financial instrument that would be significantly different if the instrument was newly originated.
- Significant changes in external market indicators of credit risk for a particular financial instrument or similar financial instrument.
- Other Information related to the borrower, such as changes in the price of a borrower's debt/equity instrument.
- An actual/expected internal credit rating downgrade for the borrower or decrease in behavioral score used to assess credit risk internally.
- Existing or forecast adverse changes in business, financial or economic condition that are expected to cause a significant change in the borrower's ability to meet its obligation.
- An Actual or expected significant change in the operating results of the borrower in relating to actual/expected decline in revenue, Increase in operating risk, working capital deficiency, Decrease in asset quality, Increase in gearing, liquidity management problems.
- Significant increase in credit risk on other financial instruments of the same borrower.
- An Actual or expected significant adverse change in the regulatory, economic or technological environment of the borrower that result in a significant change in the borrower's ability to meet the debt obligation

Grouping Financial Assets Measured on a Collective Basis

As explained above, Company calculates ECL either on a collective or individual basis. Asset classes where Company calculates ECL on an Individual basis includes All Individually significant Assets which are belong to stage 3. All assets which belong stage 1 & 2 will be assessed collectively for Impairment.

Company groups these exposures for smaller homogenous exposures, based on a combination of internal and external characteristics of the loan as described below :

- Product Type
- Type of Collateral
- Days Past Due
- Industry

The Calculation of ECL

The Company calculates ECL based on 3 probability weighted scenarios to measure expected cash shortfalls, discounted at an approximation to the EIR.

A cash shortfall is the difference between the cashflows that are due to an entity in accordance with the contract and the cash flows that the entity expects to receive.

The mechanics of the ECL calculation are outlined below and the key elements are as follows :

- PD : The Probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.
- EAD : Exposure At Default is the estimate of the exposure at a future default date, taking in to account expected changes in the exposure after the reporting date, including repayments of the principle and interest, whether scheduled by contract or otherwise, expected draw downs on committed facilities.

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- LGD : Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cashflows due and those that the lenders would expect to receive, including realization of any collateral. It is usually expressed as a % of the EAD.

When estimating the ECL, Company considers 3 scenarios (Base Case, Best Case & Worst Case). Each of these scenarios associated with different loss rates. For all products Company considers the maximum period of which the credit losses are determined is the contractual life of a financial instrument.

Forward Looking Information

In its ECL model Company relies on broad range qualitative/quantitative forward looking information as economic input such as :

Quantitative

- GDP Growth
- Inflation
- Unemployment
- Interest Rates
- Exchange Rates

Qualitative

- Government Policies
- Status of the Industry Business
- Regulatory Impact

3.10.2 SLFRS 15 - Revenue from Contracts with Customers

SLFRS 15 is effective for periods beginning on 1 January 2018 with early adoption permitted. SLFRS 15 defines principles for recognising revenue and will be applicable to all contracts with customers. However, interest and fee income integral to financial instruments and leases will continue to fall outside the scope of SLFRS 15 and will be regulated by the other applicable standards such as SLFRS 09-'Financial Instruments' and SLFRS 16-'Leases'.

Revenue under SLFRS 15 will need to be recognised as goods and services are transferred, to the extent that the transferor anticipates entitlement to goods and services. The standard will also specify a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers. The entity does not anticipate early adoption of SLFRS 15.

A preliminary evaluation of the existing contracts which falls mainly under fee and commission based income

of the Company has been performed in relation to the adoption of SLFRS 15. The Company and the Group current assessment and quantification as a result of the contract evaluation has not revealed a significant change to the revenue recognition pattern.

3.10.3 SLFRS 16 - Leases

SLFRS 16 replaces LKAS 17-'Leases', IFRIC 4-Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. SLFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under LKAS 17. At the commencement date of a lease, a lessee will recognise a liability to make lease payments and an asset representing the right to use the underlying asset during the lease term. Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to re-measure the lease liability upon the occurrence of certain events (e.g. a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the re-measurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under SLFRS 16 is substantially unchanged from today's accounting under LKAS 17. Lessors will continue to classify all leases using the same classification principle as in LKAS 17 and distinguish between two types of leases : operating and finance leases.

SLFRS 16 also requires lessees and lessors to make more extensive disclosures than under LKAS 17. SLFRS 16 is effective for annual periods beginning on or after 1 January 2019.

In 2018, the Company and the Group will continue to assess the potential effect of SLFRS 16 in its Financial Statements.

Specific Accounting Policies and Notes

This section provides specific accounting policies and accounting estimates in relation to the reported values in the Financial Statements with additional notes and explanations.

4 Income

Accounting Policy

Income is recognised to the extent that it is probable that the economic benefits will flow to the Company and the Group and revenue can be reliably measured. The specific recognition criteria, for each type of gross income given under the respective income notes.

| For the year ended 31 December | Company | | Group | |
|--|-----------------|-----------------------------|-----------------|-----------------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2017 Rs.'000 | 2016 Rs.'000 Restated |
| Interest and similar income | 6,157,286 | 4,737,774 | 6,256,612 | 4,853,007 |
| Fee and commission income | 179,687 | 131,483 | 140,151 | 190,723 |
| Insurance premium income | - | - | 562,170 | 995,321 |
| Net trading income | [16,018] | 10,072 | [13,769] | 5,612 |
| Net gain/(loss) on financial assets - held-for-trading | 5,624 | [61,096] | 4,771 | [58,226] |
| Other operating income | 76,246 | 69,922 | 129,175 | 113,561 |
| | 6,402,825 | 4,888,155 | 7,079,110 | 6,099,998 |

5 Net Interest Income

Accounting Policy

Recognition of Income and Expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

Interest and Similar Income and Expense

For all financial instruments measured at amortised cost, interest bearing financial assets classified as available-for-sale and financial instruments designated at fair value through profit or loss, interest income or expense is recorded using the EIR, which is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and an integral part of the EIR, but not future credit losses.

The carrying amount of the financial assets or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and change in carrying amount is recorded as interest income for financial assets and interest expenses for financial liabilities. However, for a re-classified financial assets for which the Group subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the EIR from the date of the change in estimate.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Overdue Interests

Interest from overdue rentals have been accounted for on a cash received basis.

Notes to the Financial Statements

5 Net Interest Income (Contd.)

| For the year ended 31 December | Company | | Group | |
|---|------------------|------------------|------------------|------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Interest and Similar Income | | | | |
| Loans and advances to customers | 5,713,336 | 4,436,037 | 5,710,885 | 4,436,037 |
| Financial investments-available-for-sale & held-to-maturity | 352,096 | 278,132 | 388,390 | 317,885 |
| Placements with banks & financial institutions | 91,854 | 23,605 | 157,337 | 99,085 |
| | 6,157,286 | 4,737,774 | 6,256,612 | 4,853,007 |
| Interest and Similar Expenses | | | | |
| Due to banks | 3,592 | 289,460 | 6,142 | 289,556 |
| Due to customers | 2,556,010 | 1,705,850 | 2,555,021 | 1,705,850 |
| Debt issued and other borrowed funds | 1,148,767 | 684,919 | 1,146,316 | 684,919 |
| Other | 439 | 29,375 | 1,146 | 30,232 |
| | 3,708,808 | 2,709,604 | 3,708,625 | 2,710,557 |
| Net Interest Income | 2,448,478 | 2,028,170 | 2,547,987 | 2,142,450 |

6 Net Fee and Commission Income

Fee and Commission Income

Accounting Policy

Fee and commission income are earned from a diverse range of services provided by the Group to its customers. Fees and commission income are accounted for as follows:

- Income earned on the execution of a significant act is recognised as revenue when the act is completed; and
- Income earned from the provision of services is recognised as revenue as the services are provided.

| For the year ended 31 December | Company | | Group | |
|--------------------------------------|-----------------|-----------------------------|-----------------|-----------------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2017 Rs.'000 | 2016 Rs.'000 Restated |
| Fee and Commission Income | | | | |
| Trade & other related activities | 179,687 | 131,483 | 173,620 | 114,600 |
| Reinsurance commission income | - | - | [37,051] | 61,214 |
| Others | - | - | 3,582 | 14,909 |
| | 179,687 | 131,483 | 140,151 | 190,723 |
| Fee and Commission Expenses | | | | |
| Fees | 59,964 | 37,813 | 77,707 | 103,487 |
| | 59,964 | 37,813 | 77,707 | 103,487 |
| Net Fee and Commission Income | 119,723 | 93,670 | 62,444 | 87,236 |

7 Insurance Premium Income

Accounting Policy

Gross Premiums

Gross recurring premiums on life and investment contracts with Discretionary Participation Features (DPF) are recognised as revenue when receivable from the policy holder. For single premium business, revenue is recognised on the date on which the policy is effective.

Gross general insurance written premiums comprise the total premiums receivable for the whole period of cover provided by contracts entered during the accounting period and are recognised on the date on which the policy commences.

Unearned premium reserve represents the portion of the premium written in the year but relating to the unexpired term of coverage. Unearned premiums are calculated on the 1/24 basis.

Reinsurance Premiums

Gross reinsurance premiums on life and investment contracts are recognised as an expense from the date on which the policy is effective.

Gross general reinsurance premiums written comprise the total premiums payable for the whole cover provided by contracts entered in to the period and are recognised on the date on which the policy incept. Premiums include any adjustments arising in the accounting period in respect of reinsurance contracts incepting in prior accounting periods.

Unearned reinsurance premiums are those proportions of premiums written in a year that relate to periods of risk after the reporting date. Unearned reinsurance premiums are deferred over the term of the underlying direct insurance policies for risks-attaching contracts and over the term of the reinsurance contract for losses occurring contracts.

Benefits, Claims and Expenses Recognition

Gross Benefits and Claims

Gross benefits and claims for life insurance contracts and for investment contracts with DPF include the cost of all claims arising during the year including internal and external claims handling costs that are directly related to the processing and settlement of claims and policyholder bonuses declared on DPF contracts, as well as changes in the gross valuation of insurance and investment contract liabilities with DPF. Death claims and surrenders are recorded on the basis of notifications received. Maturities and annuity payments are recorded when due. Interim payments and surrenders are accounted at the time of settlement.

General insurance includes all claims occurring during the year, whether reported or not, related internal and external claims handling costs that are directly related to the processing and settlement of claims, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years.

Claims expenses and liabilities for outstanding claims are recognised in respect of direct and inward reinsurance business. The liability covers claims reported but not yet paid, Incurred But Not Reported claims (IBNR) and the anticipated direct and indirect costs of settling those claims. Claims outstanding are assessed by review of individual claim files and estimating changes in the ultimate cost of settling claims. The provision in respect of IBNR is actuarially valued on an annual basis to ensure a more realistic estimation of the future liability based on past experience and trends.

While the Directors consider that the provision for claims is fairly stated on the basis of information currently available, the ultimate liability will vary as a result of subsequent information and events. This may result in adjustment to the amounts provided. Such amounts are reflected in the Financial Statements for that period. The methods used, and the estimates made are reviewed regularly.

Notes to the Financial Statements

7 Insurance Premium Income (Contd.)

Reinsurance Claims

Reinsurance claims are recognised when the related gross insurance claim is recognised according to the terms of the relevant contract.

| For the year ended 31 December | Group | |
|--|-----------------|------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Non-life insurance | 243,964 | 998,991 |
| Life insurance | 123,732 | 235,533 |
| Total gross written premium | 367,696 | 1,234,524 |
| Change in unearned premium provisions | 292,198 | 29,441 |
| Gross premium income | 659,894 | 1,263,965 |
| Less: Premium ceded to reinsurers | 97,724 | 268,644 |
| Net premium income | 562,170 | 995,321 |

8 Net Trading Income

Accounting Policy

Results arising from trading activities include dividends from financial assets and gain/(loss) on disposal of financial assets - held-for-trading.

| For the year ended 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Dividend income | 8,278 | 12,853 | 9,440 | 13,127 |
| Gain/(loss) on disposal of quoted shares | (24,296) | (2,781) | (23,209) | (7,515) |
| Net trading income | (16,018) | 10,072 | (13,769) | 5,612 |

9 Net Gain/(Loss) on Financial Assets - Held-for-Trading

Accounting Policy

Fair value gains and losses attributable to changes in the fair values of the equity and debt securities classified under financial assets held-for-trading is recognised in the Statement of Profit or Loss, when there is a change to the fair value of the asset.

| For the year ended 31 December | Company | | Group | |
|-----------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Financial assets held-for-trading | 5,624 | (61,096) | 4,771 | (58,226) |
| | 5,624 | (61,096) | 4,771 | (58,226) |

10 Other Operating Income

Accounting Policy

Other operating income includes gains on disposal of property & equipment, dividend income, profit & losses from real estates and gains from sale of available-for-sale financial investments.

Gain from Sale of Available-for-Sale Financial Investments

Gains from sale of available-for-sale financial investments are the amounts transferred from equity to the Statement of Profit or Loss on the derecognition of investments classified as available-for-sale investments.

Dividend Income

Dividend income shall be recognised when the Group's right to receive payment is established.

| For the year ended 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Profit/(loss) on sale of property & equipment including foreclosed properties | 3,654 | 32,909 | 4,718 | 35,990 |
| Other income | 72,592 | 37,013 | 124,457 | 77,571 |
| | 76,246 | 69,922 | 129,175 | 113,561 |

11 Impairment Charges for Loans and Other Losses

Accounting Policy

The Company and Group recognises the changes in the impairment provisions for loans and receivables which are assessed as per Sri Lanka Accounting Standard-LKAS 39-'Financial Instruments: Recognition and Measurement'. The methodology adopted by the Company and the Group is explained in note 21 to these Financial Statements.

| For the year ended 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Loans and advances to customers | | | | |
| Bills receivables | (233) | 16,018 | (233) | 16,018 |
| Loans & advances to customers | 130,033 | (15,612) | 130,033 | (15,612) |
| Lease and hire purchase rental receivables | 114,431 | 23,833 | 114,431 | 23,833 |
| Insurance receivables | - | - | 975 | 3,720 |
| | 244,231 | 24,239 | 245,206 | 27,959 |

Notes to the Financial Statements

12 Personnel Expenses

Accounting Policy

Personnel expenses include salaries, bonus, terminal benefit charges and other related expenses. The provision for bonus is recognised when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made on the amount of obligation.

Defined Contribution Plan – Employees’ Provident Fund and Employees’ Trust Fund (EPF & ETF)

Employees are eligible for Employees’ Provident Fund contributions and Employees’ Trust Fund contributions in line with respective statutes and regulations. The Group and employees contribute 12% and 8% of gross emoluments of employees to Employee’s Provident Fund. The Group contribute 3% of gross emoluments of employees to the Employees’ Trust Fund.

| For the year ended 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Staff emoluments | 706,356 | 629,301 | 822,797 | 783,808 |
| Employers' contribution to defined contribution plans | | | | |
| Employees' Provident Fund | 71,956 | 59,175 | 86,860 | 79,345 |
| Employees' Trust Fund | 18,603 | 14,794 | 22,323 | 19,833 |
| Other personnel expenses | 230,177 | 78,260 | 247,679 | 110,098 |
| | 1,027,092 | 781,530 | 1,179,659 | 993,084 |

13 Other Operating Expenses

Accounting Policy

Other operating expenses are recognised in the Statement of Profit or Loss on the basis of a direct association between the cost incurred and the earning of specific items of income. All expenditure incurred in the running of the business and in maintaining the property & equipment in a state of efficiency has been charged to the Statement of Profit or Loss in arriving at that profit for the year.

Nation Building Tax (NBT) on Financial Services

NBT on financial services is calculated in accordance with Nation Building Tax (NBT) Act No 9 of 2009 and subsequent amendments thereto with effect from 01st January 2014. NBT on financial services is calculated as 2% of the value addition used for the purpose of Value Added Tax (VAT) on financial Services.

| For the year ended 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Directors' emoluments | 6,301 | 4,123 | 6,699 | 7,367 |
| Auditors' remuneration | | | | |
| Audit fees | 1,881 | 1,918 | 2,686 | 2,723 |
| Non audit fees | 653 | 625 | 653 | 833 |
| Professional & legal fees | 28,449 | 27,537 | 44,749 | 42,283 |
| Donations | 38 | 197 | 3,038 | 222 |
| Office administration & establishment expenses | 288,557 | 241,974 | 360,361 | 318,268 |
| Other | 417,150 | 365,566 | 504,873 | 543,479 |
| | 743,029 | 641,940 | 923,059 | 915,175 |

14 Income Tax Expense

Accounting Policy

Current Tax

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

Accordingly, provision for taxation is based on the profit for the year adjusted for taxation purposes in accordance with the provisions of the Inland Revenue Act No. 10 of 2006 and the amendments thereto. The Company and its subsidiary are liable for income tax on profit from operations is calculated at the rate of 28%.

| For the year ended 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Current Tax | | | | |
| Current income tax | [54,966] | 62,838 | [46,653] | 74,249 |
| Deferred Tax | | | | |
| Relating to origination and reversal of temporary differences | | | | |
| Statement of Profit or Loss | 182,765 | 91,409 | 182,765 | 91,409 |
| Statement of Other Comprehensive Income | [15,942] | 1,810 | [15,942] | 1,810 |
| | 111,857 | 156,057 | 120,170 | 167,468 |
| Tax charged to Statement of Profit or Loss | 127,799 | 154,247 | 136,112 | 165,658 |
| Tax charged/(reversed) to Statement of Other Comprehensive Income | [15,942] | 1,810 | [15,942] | 1,810 |
| | 111,857 | 156,057 | 120,170 | 167,468 |
| Effective tax rate [excluding deferred tax] % | [24.04] | 26.98 | [19.48] | 30.96 |
| Effective tax rate % | 55.89 | 66.23 | 56.84 | 69.07 |

Notes to the Financial Statements

14 Income Tax Expense (Contd.)

Reconciliation of the Total Tax Charged

A reconciliation between the tax expense and the accounting profit multiplied by statutory tax rate for the years ended 31 December is as follows:

| For the year ended 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Profit as per statement of Profit or Loss | 228,650 | 232,897 | 239,461 | 239,826 |
| Add : Disallowable expenses | 525,760 | 573,332 | 525,760 | 611,530 |
| Add : Lease capital recoverable | 9,475,875 | 7,545,620 | 9,475,875 | 7,545,620 |
| Less : Allowable expenses | 7,184,700 | 5,865,789 | 7,184,700 | 5,981,532 |
| Less : Exempted/allowable income | 2,669,150 | 1,994,681 | 2,669,150 | 2,020,095 |
| Statutory income | 376,435 | 491,379 | 387,246 | 395,349 |
| Less : Tax loss set off | 250,393 | 264,750 | 250,393 | [10,855] |
| Assessable income | 126,042 | 226,629 | 136,853 | 496,204 |
| Taxable income | 126,042 | 224,421 | 151,551 | 262,473 |
| At the effective income tax rate | 35,292 | 62,838 | 42,435 | 73,492 |
| (Over)/under provision - Previous years | [90,258] | - | [90,258] | - |
| Current tax on profits for the year | [54,966] | 62,838 | [47,823] | 73,492 |
| Deffered tax charged/(reversal) for the year | 182,765 | 91,409 | 182,765 | 91,409 |
| Share of associate company's current tax | - | - | 1,170 | 758 |
| Tax expense for the year | 127,799 | 154,247 | 136,112 | 165,658 |
| Deferred tax charge/ (reversal) to Statement of Other Comprehensive Income | [15,942] | 1,810 | [15,942] | 1,810 |
| Total income tax expense | 111,857 | 156,057 | 120,170 | 167,468 |

15 Earnings Per Share and Dividend Per Share

15.1 Basic Earnings Per Share

Accounting Policy

Basic EPS is calculated by dividing the profit attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the Year.

Diluted EPS is determined by adjusting the profit attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

| For the year ended 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Profit attributable to ordinary shareholders (Rs.'000) | 100,851 | 78,650 | 111,858 | 110,879 |
| Number of ordinary shares used as denominator ('000) | 165,875 | 165,875 | 165,875 | 165,875 |
| Basic earnings per ordinary share (Rs.) | 0.61 | 0.47 | 0.67 | 0.67 |

15.2 Dividend Per Share

No dividend has been declared and paid by the Company and the Group during the year 2017 and 2016.

16 Analysis of Financial Instruments by Measurement Basis

Accounting Policy

Financial instruments are measured on an ongoing basis either at fair value or at amortised cost. The summary of significant accounting policies describes how each category of financial instruments is measured and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the carrying amounts of financial instruments by category as defined in Sri Lanka Accounting Standard-LKAS 39-‘Financial Instruments: Recognition and Measurement’ under heading of the Statement of Financial Position.

16.1 Company - 2017

| | Held-for -Trading [FVPL] | Available -for-Sale [AFS] | Loans and Receivables [L & R] | Held-to -Maturity [HTM] | Rs.'000 Total |
|--|--------------------------------|---------------------------------|-------------------------------------|---|------------------|
| Assets | | | | | |
| Cash and cash equivalents | - | - | 418,885 | - | 418,885 |
| Placements with banks & financial institutions | - | - | 1,509,597 | - | 1,509,597 |
| Securities purchased under resale agreements | - | - | 1,302,748 | - | 1,302,748 |
| Financial investments - held-for-trading | 231,264 | - | - | - | 231,264 |
| Bills receivable | - | - | 494,096 | - | 494,096 |
| Loans & advances to customers | - | - | 12,598,133 | - | 12,598,133 |
| Lease and hire purchase receivable | - | - | 15,661,432 | - | 15,661,432 |
| Financial investments - available-for-sale | - | 1,815,181 | - | - | 1,815,181 |
| Financial investments - held-to-maturity | - | - | - | 479,362 | 479,362 |
| Other assets | - | - | 46,865 | - | 46,865 |
| Total financial assets | 231,264 | 1,815,181 | 32,031,756 | 479,362 | 34,557,563 |
| Liabilities | | | | | |
| | | | | Financial Liabilities at Amortised Cost | Total |
| Due to banks | | | | 123,849 | 123,849 |
| Securities sold under repurchase agreements | | | | 437,672 | 437,672 |
| Due to customers | | | | 21,918,869 | 21,918,869 |
| Debt issued and borrowed funds | | | | 8,818,862 | 8,818,862 |
| Other liabilities | | | | 338,072 | 338,072 |
| Total financial liabilities | | | | 31,637,324 | 31,637,324 |

Notes to the Financial Statements

16 Analysis of Financial Instruments by Measurement Basis (Contd.)

16.2 Company - 2016

| | Held-for -Trading [FVPL] | Available -for-Sale [AFS] | Loans and Receivables [L & R] | Held-to -Maturity [HTM] | Rs.'000 Total |
|--|--------------------------------|---------------------------------|-------------------------------------|---|-------------------|
| Assets | | | | | |
| Cash and cash equivalents | - | - | 401,301 | - | 401,301 |
| Placements with banks & financial institutions | - | - | 118,933 | - | 118,933 |
| Securities purchased under resale agreements | - | - | 265,687 | - | 265,687 |
| Financial investments - held-for-trading | 323,655 | - | - | - | 323,655 |
| Bills receivable | - | - | 739,403 | - | 739,403 |
| Loans & advances to customers | - | - | 11,320,845 | - | 11,320,845 |
| Lease and hire purchase receivable | - | - | 14,991,751 | - | 14,991,751 |
| Financial investments - available-for-sale | - | 2,735,645 | - | - | 2,735,645 |
| Financial investments - held-to-maturity | - | - | - | 57,766 | 57,766 |
| Other assets | - | - | 34,454 | - | 34,454 |
| Total financial assets | 323,655 | 2,735,645 | 27,872,374 | 57,766 | 30,989,440 |
| | | | | Financial Liabilities at Amortised Cost | Total |
| Liabilities | | | | | |
| Due to banks | | | | 201,635 | 201,635 |
| Securities sold under repurchase agreements | | | | 401,820 | 401,820 |
| Due to customers | | | | 18,518,419 | 18,518,419 |
| Debt issued and borrowed funds | | | | 8,722,787 | 8,722,787 |
| Other liabilities | | | | 110,717 | 110,717 |
| Total financial liabilities | | | | 27,955,378 | 27,955,378 |

16.3 Group - 2017

| | Held-for -Trading [FVPL] | Available -for-Sale [AFS] | Loans and Receivables [L & R] | Held-to -Maturity [HTM] | Rs.'000 Total |
|--|--------------------------------|---------------------------------|-------------------------------------|---|-------------------|
| Assets | | | | | |
| Cash and cash equivalents | - | - | 466,139 | - | 466,139 |
| Placements with banks & financial institutions | - | - | 1,597,785 | - | 1,597,785 |
| Securities purchased under resale agreements | - | - | 1,651,927 | - | 1,651,927 |
| Financial investments - held-for-trading | 238,252 | - | - | - | 238,252 |
| Bills receivable | - | - | 494,096 | - | 494,096 |
| Loans & advances to customers | - | - | 12,592,956 | - | 12,592,956 |
| Lease and hire purchase receivable | - | - | 15,661,432 | - | 15,661,432 |
| Financial investments - available-for-sale | - | 2,191,842 | - | - | 2,191,842 |
| Financial investments - held-to-maturity | - | - | - | 479,362 | 479,362 |
| Other assets | - | - | 46,865 | - | 46,865 |
| Total financial assets | 238,252 | 2,191,842 | 32,511,200 | 479,362 | 35,420,656 |
| | | | | Financial Liabilities at Amortised Cost | Total |
| Liabilities | | | | | |
| Due to banks | | | | 129,877 | 129,877 |
| Securities sold under repurchase agreements | | | | 437,672 | 437,672 |
| Due to customers | | | | 21,910,383 | 21,910,383 |
| Debt issued and borrowed funds | | | | 8,818,862 | 8,818,862 |
| Other liabilities | | | | 338,072 | 338,072 |
| Total financial liabilities | | | | 31,634,866 | 31,634,866 |

Notes to the Financial Statements

16.4 Group - 2016

| | Held-for- Trading [FVPL] | Available -for-Sale [AFS] | Loans and Receivables [L & R] | Held-to- Maturity [HTM] | Rs.'000 Total |
|--|--------------------------------|---------------------------------|-------------------------------------|---|-------------------|
| Assets | | | | | |
| Cash and cash equivalents | - | - | 441,357 | - | 441,357 |
| Placements with banks & financial institutions | - | - | 262,319 | - | 262,319 |
| Securities purchased under resale agreements | - | - | 730,773 | - | 730,773 |
| Financial investments - held-for-trading | 331,586 | - | - | - | 331,586 |
| Bills receivable | - | - | 739,403 | - | 739,403 |
| Loans & advances to customers | - | - | 11,392,491 | - | 11,392,491 |
| Lease and hire purchase receivable | - | - | 14,991,751 | - | 14,991,751 |
| Financial investments - available-for-sale | - | 3,126,815 | - | - | 3,126,815 |
| Financial investments - held-to-maturity | - | - | - | 57,766 | 57,766 |
| Other assets | - | - | 34,454 | - | 34,454 |
| Total financial assets | 331,586 | 3,126,815 | 28,592,548 | 57,766 | 32,108,715 |
| | | | | Financial Liabilities at Amortised Cost | Total |
| Liabilities | | | | | |
| Due to banks | | | | 224,997 | 224,997 |
| Securities sold under repurchase agreements | | | | 401,820 | 401,820 |
| Due to customers | | | | 18,518,419 | 18,518,419 |
| Debt issued and borrowed funds | | | | 8,722,787 | 8,722,787 |
| Other liabilities | | | | 110,717 | 110,717 |
| Total financial liabilities | | | | 27,978,740 | 27,978,740 |

17 Cash and Cash Equivalents

Accounting Policy

Cash and cash equivalents include cash in hand, demand deposits and short-term highly liquid investments which are readily convertible to known amounts of cash and are subject to insignificant risk of changes in value. There were no cash and cash equivalent balances held by the Group companies that were not available for use by the Group. Cash & cash equivalents are carried at amortised cost.

| As at 31 December | Company | | Group | |
|-------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Cash in hand | 188,113 | 183,510 | 188,113 | 183,510 |
| Cash at bank | 230,772 | 217,791 | 278,026 | 257,847 |
| | 418,885 | 401,301 | 466,139 | 441,357 |

18 Placements with Banks & Financial Institutions

Accounting Policy

Balances with banks & financial institutions includes fixed deposits and other deposits in local currency. Balances with banks & financial institution are carried at amortised cost in the Statement of Financial Position.

| As at 31 December | Company | | Group | |
|-------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Fixed deposits | 1,509,597 | 118,933 | 1,597,785 | 262,319 |
| | 1,509,597 | 118,933 | 1,597,785 | 262,319 |

19 Securities Sold Under Repurchase Agreements

Securities sold under agreements to repurchase at a specified future date are not de-recognised from the Statement of Financial Position as the Group retains substantially all the risks and rewards of ownership. The corresponding cash received is recognised in the Consolidated Statement of Financial Position as a liability with a corresponding obligation to return it, including accrued interest as a liability within 'Securities sold under repurchase agreements', reflecting the transaction's economic substance as a loan to the Group. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of agreement using the EIR.

Securities Purchased Under Resale Agreements

Securities purchased under agreements to resell at a specified future date are not recognised in the Statement of Financial Position. The consideration paid, including accrued interest, is recorded in the Statement of Financial Position, within 'Securities purchased under resale agreements', reflecting the transaction's economic substance as a loan by the Group. The difference between the purchase and resale prices is recorded in 'Net interest income' and is accrued over the life of the agreement using the EIR.

| As at 31 December | Company | | Group | |
|-------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| 19.1 Assets | | | | |
| Repurchased agreements | 1,302,748 | 265,687 | 1,651,927 | 730,773 |
| | 1,302,748 | 265,687 | 1,651,927 | 730,773 |
| 19.2 Liabilities | | | | |
| Reverse repurchase agreements | 437,672 | 401,820 | 437,672 | 401,820 |
| | 437,672 | 401,820 | 437,672 | 401,820 |

20 Financial Investments - Held-for-Trading

Financial investments are classified as held-for-trading if they are acquired principally for the purpose of selling or repurchasing in the near term or holds as a part of a portfolio that is managed together for short-term profit or position taking. Financial assets held-for-trading are recorded in the Statement of Financial Position at fair value. Changes in fair value are recognised in 'Net trading income'. Interest and dividend income or expenses is recorded in 'Net trading income' according to the terms of the contract, or when the right to receive the payment has been established.

Financial investments held-for-trading include debt securities and equities that have been acquired principally for the purpose of selling or repurchasing in the near term.

Notes to the Financial Statements

20 Financial Investments - Held-for-Trading (Contd.)

| As at 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Quoted equities and unit trusts (Note 20.1) | 226,651 | 321,420 | 233,639 | 329,351 |
| Debt securities (Note 20.2) | 4,613 | 2,235 | 4,613 | 2,235 |
| | 231,264 | 323,655 | 238,252 | 331,586 |

20.1 Quoted Equities and Unit Trusts

| | 2017 | | | 2016 | | |
|---|-----------------|--------------------------|--------------------------|-----------------|--------------------------|--------------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Company | | | | | | |
| Bank, Finance and Insurance | | | | | | |
| Amana Takaful PLC | 500,000 | 450 | 400 | - | - | - |
| Asia Asset Finance PLC | 639,289 | 1,023 | 895 | - | - | - |
| Central Finance Company PLC | 46,331 | 5,842 | 4,276 | 45,000 | 5,842 | 4,500 |
| Ceylinco Insurance PLC | - | - | - | 1,810 | 2,851 | 2,697 |
| Citizens Development Business Finance PLC-Non Voting | 44,733 | 3,992 | 2,505 | 44,733 | 3,992 | 2,778 |
| Commercial Bank Of Ceylon PLC | - | - | - | 9,964 | 1,714 | 1,445 |
| Commercial Bank Of Ceylon PLC-Non Voting | 40,000 | 4,202 | 4,200 | - | - | - |
| Commercial Credit and Finance PLC | 22,500 | 1,498 | 968 | 30,000 | 1,998 | 1,689 |
| DFCC Bank PLC | 120,000 | 24,993 | 14,736 | 120,000 | 24,993 | 14,700 |
| HNB Assurance PLC | - | - | - | 7,500 | 621 | 441 |
| Housing Development Finance Corporation Bank of Sri Lanka | - | - | - | 26,500 | 1,832 | 1,251 |
| Janashakthi Insurance Company PLC | 669,893 | 12,975 | 10,517 | 674,893 | 13,072 | 11,066 |
| L B Finance PLC | 12,500 | 1,645 | 1,526 | - | - | - |
| Lanka Orix Leasing Company PLC | - | - | - | 133,100 | 15,180 | 9,650 |
| LQLC Finance PLC | - | - | - | 500,000 | 1,300 | 1,300 |
| National Development Bank PLC | 74,286 | 16,253 | 10,133 | 72,704 | 16,513 | 11,342 |
| Nations Trust Bank PLC | 210,032 | 20,648 | 16,382 | 210,032 | 20,657 | 16,992 |
| Pan Asia Banking Corporation PLC | 30,000 | 516 | 471 | - | - | - |
| Sanasa Development Bank PLC | 18,152 | 1,828 | 1,849 | 256 | 27 | 27 |
| Seylan Bank PLC | 137,789 | 13,846 | 12,015 | 135,000 | 13,846 | 12,150 |
| Seylan Bank PLC-Non Voting | 341,439 | 17,845 | 19,121 | 330,000 | 17,845 | 19,470 |
| Softlogic Finance PLC | 60,515 | 3,340 | 2,203 | 60,515 | 3,340 | 2,058 |
| The Finance Company PLC | 200,000 | 973 | 440 | 200,000 | 973 | 580 |
| Union Bank Of Colombo PLC | - | - | - | 10,000 | 170 | 154 |
| | | 131,869 | 102,637 | | 146,766 | 114,290 |

| | 2017 | | | 2016 | | |
|---|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Beverage, Food and Tobacco | | | | | | |
| Bairaha Farms PLC | 25,000 | 3,962 | 3,683 | - | - | - |
| HVA Foods PLC | 25,000 | 155 | 153 | - | - | - |
| Keells Food Products PLC | 27,672 | 4,746 | 3,874 | 27,672 | 4,746 | 4,372 |
| Lion Brewery Ceylon PLC | 672 | 370 | 363 | - | - | - |
| Lucky Lanka Milk Processing Company PLC | 2,657,487 | 15,808 | 5,049 | 2,657,487 | 15,808 | 8,504 |
| Renuka Agri Foods PLC | 752,274 | 3,091 | 1,956 | 752,274 | 3,091 | 2,182 |
| | | 28,132 | 15,078 | | 23,645 | 15,058 |
| Chemical & Pharmaceuticals | | | | | | |
| CIC Holdings PLC | 2,000 | 144 | 124 | - | - | - |
| CIC Holdings PLC-Non Voting | 25,164 | 1,483 | 1,193 | 7,500 | 585 | 510 |
| | | 1,627 | 1,317 | | 585 | 510 |
| Construction and Engineering | | | | | | |
| Colombo Dockyard PLC | - | - | - | 17,918 | 3,537 | 1,408 |
| MTD Walkers PLC | 130,000 | 7,745 | 3,003 | 130,000 | 7,745 | 5,330 |
| | | 7,745 | 3,003 | | 11,282 | 6,738 |
| Diversified | | | | | | |
| Dunamis Capital PLC | 27,500 | 719 | 644 | - | - | - |
| Taprobane Holdings PLC | 30,000 | 180 | 165 | - | - | - |
| | | 899 | 809 | | - | - |
| Diversified Holdings | | | | | | |
| Aitken Spence PLC | 110,000 | 11,110 | 6,006 | 115,000 | 11,616 | 7,475 |
| Browns Investments PLC | 750,000 | 2,475 | 1,950 | - | - | - |
| Hayleys PLC | 500 | 142 | 121 | - | - | - |
| John Keells Holdings PLC | 15,000 | 2,175 | 2,228 | 264,627 | 42,826 | 38,371 |
| Melstacorp PLC | 5,000 | 305 | 298 | 600,000 | 28,973 | 35,580 |
| Sunshine Holdings PLC | 35,211 | 2,119 | 2,007 | - | - | - |
| The Colombo Fort Land & Building PLC | 44,799 | 1,224 | 851 | 45,000 | 1,230 | 900 |
| Vallibel One PLC | 50,000 | 950 | 885 | - | - | - |
| | | 20,500 | 14,346 | | 84,645 | 82,326 |
| Footwear & Textiles | | | | | | |
| Hayleys Fabric PLC | 100,000 | 1,700 | 1,350 | - | - | - |
| Ceylon Leather Products PLC | 8,000 | 615 | 483 | 11,348 | 873 | 794 |
| | | 2,315 | 1,833 | | 873 | 794 |

Notes to the Financial Statements

20 Financial Investments - Held-for-Trading (Contd.)

| | 2017 | | | 2016 | | |
|------------------------------------|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Health Care | | | | | | |
| Ceylon Hospitals PLC (Durdans) | 5,000 | 500 | 415 | - | - | - |
| | | 500 | 415 | | - | - |
| Hotels and Travels | | | | | | |
| Aitken Spence Hotel Holdings PLC | 63,219 | 5,779 | 1,865 | 63,219 | 5,793 | 2,725 |
| Asian Hotels & Properties PLC | - | - | - | 132,817 | 9,938 | 7,571 |
| Beruwala Resorts PLC | 100,000 | 100 | 80 | - | - | - |
| Ceylon Hotels Corporation PLC | - | - | - | 2,930 | 75 | 59 |
| Eden Hotel Lanka PLC | 127,743 | 3,676 | 1,813 | 127,743 | 3,677 | 1,725 |
| Galadari Hotels (Lanka) PLC | - | - | - | 20,000 | 292 | 214 |
| John Keells Hotels PLC | 75,000 | 1,175 | 660 | 75,000 | 1,175 | 818 |
| Marawila Resorts PLC | - | - | - | 959,168 | 4,606 | 2,302 |
| Palm Garden Hotels PLC | 147,472 | 10,890 | 3,849 | 147,472 | 10,927 | 4,173 |
| The Kingsbury PLC | 1,937,727 | 41,834 | 26,159 | 1,937,727 | 41,846 | 29,454 |
| Waskaduwa Beach Resort PLC | 50,000 | 245 | 190 | 50,000 | 306 | 220 |
| | | 63,699 | 34,616 | | 78,635 | 49,261 |
| Information and Technology | | | | | | |
| E-Channelling PLC | 15,000 | 120 | 89 | - | - | - |
| | | 120 | 89 | | - | - |
| Investment Trust | | | | | | |
| Ceylon Investment PLC | 65,727 | 6,411 | 2,938 | 91,164 | 8,893 | 4,475 |
| Lanka Century Investments PLC | 500,000 | 6,891 | 6,050 | 520,000 | 7,167 | 6,136 |
| Renuka Holdings PLC | - | - | - | 106,441 | 4,266 | 2,246 |
| | | 13,302 | 8,988 | | 20,326 | 12,857 |
| Land and Property | | | | | | |
| Cargo Boat Development Company PLC | 9,984 | 899 | 839 | - | - | - |
| Commercial Development Company PLC | 4,649 | 451 | 325 | 4,649 | 451 | 349 |
| East West Properties PLC | 8,000 | 120 | 90 | - | - | - |
| R I L Property PLC | 25,000 | 200 | 180 | - | - | - |
| Seylan Developments PLC | 75,000 | 1,125 | 1,020 | - | - | - |
| | | 2,795 | 2,454 | | 451 | 349 |

| | 2017 | | | 2016 | | |
|-------------------------------|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Manufacturing | | | | | | |
| Abans Electricals PLC | 5,000 | 521 | 422 | - | - | - |
| ACL Cables PLC | 50,000 | 2,755 | 2,120 | - | - | - |
| ACME Printing & Packaging PLC | - | - | - | 131,023 | 1,137 | 812 |
| Alufab PLC | 60,000 | 1,660 | 1,380 | - | - | - |
| Central Industries PLC | - | - | - | 5,000 | 250 | 248 |
| Ceylon Grain Elevators PLC | 60,000 | 4,186 | 3,966 | - | - | - |
| Chevron Lubricants Lanka PLC | 35,000 | 4,656 | 4,165 | - | - | - |
| Dankotuwa Porcelain PLC | - | - | - | 630,902 | 6,301 | 4,479 |
| Kelani Tyres PLC | 115,000 | 9,023 | 5,106 | 115,000 | 9,023 | 7,464 |
| Lanka Tiles PLC | - | - | - | 48,253 | 5,786 | 4,627 |
| Pelwatte Sugar Industries PLC | 41,600 | 1,799 | 978 | 41,600 | 1,799 | 978 |
| Piramal Glass Ceylon PLC | - | - | - | 800,000 | 5,100 | 4,240 |
| Richard Pieris Exports PLC | 2,000 | 470 | 354 | - | - | - |
| Royal Ceramics Lanka PLC | 68,323 | 8,740 | 7,823 | - | - | - |
| Sierra Cables PLC | 1,390,000 | 6,157 | 3,475 | 1,390,000 | 6,157 | 4,587 |
| Teejay Lanka PLC | 75,000 | 2,775 | 2,550 | - | - | - |
| | | 42,742 | 32,339 | | 35,553 | 27,435 |
| Motors | | | | | | |
| United Motors Lanka PLC | 25,000 | 2,025 | 1,950 | - | - | - |
| | | 2,025 | 1,950 | | - | - |
| Plantations | | | | | | |
| Balangoda Plantations PLC | - | - | - | 497,486 | 14,996 | 6,069 |
| Elpitiya Plantations PLC | 50,000 | 1,497 | 1,410 | - | - | - |
| Kotagala Plantations PLC | - | - | - | 67,444 | 2,644 | 600 |
| | | 1,497 | 1,410 | | 17,640 | 6,669 |
| Power and Energy | | | | | | |
| Laugfs Gas PLC | 75,000 | 1,963 | 1,762 | 26,088 | 1,008 | 858 |
| Laugfs Gas PLC-Non Voting | 25,000 | 966 | 500 | - | - | - |
| Resus Energy PLC | 300 | 6 | 5 | - | - | - |
| Vallibel Power Erathna PLC | 125,000 | 975 | 937 | 50,000 | 459 | 440 |
| | | 3,910 | 3,204 | | 1,467 | 1,298 |
| Service | | | | | | |
| Ceylon Tea Brokers PLC | 114,778 | 557 | 494 | 192,655 | 937 | 751 |
| Renuka Capital PLC | 50,000 | 288 | 225 | - | - | - |
| | | 845 | 719 | | 937 | 751 |

Notes to the Financial Statements

20 Financial Investments - Held-for-Trading (Contd.)

| | 2017 | | | 2016 | | |
|--|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Telecommunication | | | | | | |
| Dialog Axiata PLC | - | - | - | 100,000 | 1,149 | 1,050 |
| | | | | | 1,149 | 1,050 |
| Trading | | | | | | |
| Brown & Company PLC | 19,061 | 1,610 | 1,344 | 5,178 | 526 | 435 |
| Eastern Merchants PLC | - | - | - | 257,922 | 2,179 | 1,599 |
| Tess Agro PLC-Non Voting | 100,000 | 130 | 100 | - | - | - |
| | | 1,740 | 1,444 | | 2,705 | 2,034 |
| Total value of quoted equities and unit trusts | | 326,262 | 226,651 | | 426,659 | 321,420 |
| 20.2 Other Debt Securities | | | | | | |
| Commercial Credit & Finance PLC | 20,000 | 2,141 | 2,325 | 20,000 | 2,141 | 2,235 |
| Hatton National Bank PLC | 26,000 | 2,377 | 2,288 | - | - | - |
| Total value of listed debentures | | 4,518 | 4,613 | | 2,141 | 2,235 |
| Total value of financial assets at fair value through profit or loss | | 330,780 | 231,264 | | 428,800 | 323,655 |
| Marked to market valuation loss | | [99,516] | | | [105,145] | |
| Fair value of financial assets designated at fair value through profit or loss | | 231,264 | | | 323,655 | |
| 20.1 Quoted Equities and Unit Trusts | | | | | | |
| Group | | | | | | |
| Bank, Finance and Insurance | | | | | | |
| Amana Takaful PLC | 500,000 | 450 | 400 | - | - | - |
| Asia Asset Finance PLC | 639,289 | 1,023 | 895 | - | - | - |
| Central Finance Company PLC | 46,331 | 5,842 | 4,276 | 45,000 | 5,842 | 4,500 |
| Ceylinco Insurance PLC | - | - | - | 1,810 | 2,851 | 2,697 |
| Chilaw Finance PLC | - | - | - | 3,753 | 87 | 77 |
| Citizens Development Business Finance PLC-Non Voting | 44,733 | 3,992 | 2,505 | 44,733 | 3,992 | 2,778 |
| Commercial Bank of Ceylon PLC | - | - | - | 9,964 | 1,714 | 1,445 |
| Commercial Bank of Ceylon PLC-Non Voting | 40,000 | 4,202 | 4,200 | - | - | - |
| Commercial Credit and Finance PLC | 22,500 | 1,498 | 968 | 30,000 | 1,998 | 1,689 |
| DFCC Bank PLC | 120,000 | 24,993 | 14,736 | 120,000 | 24,993 | 14,700 |
| HNB Assurance PLC | - | - | - | 7,500 | 621 | 441 |
| Housing Development Finance Corporation Bank of Sri Lanka | - | - | - | 26,500 | 1,832 | 1,251 |
| Janashakthi Insurance Company PLC | 669,893 | 12,975 | 10,517 | 674,893 | 13,072 | 11,068 |
| L B Finance PLC | 12,500 | 1,645 | 1,526 | - | - | - |

| | 2017 | | | 2016 | | |
|---|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Lanka Orix Leasing Company PLC | - | - | - | 133,100 | 15,180 | 9,650 |
| LOLC Finance PLC | - | - | - | 500,000 | 1,300 | 1,300 |
| National Development Bank PLC | 74,286 | 16,253 | 10,133 | 72,704 | 16,513 | 11,342 |
| Nations Trust Bank PLC | 210,032 | 20,648 | 16,382 | 210,032 | 20,657 | 16,992 |
| Pan Asia Banking Corporation PLC | 30,000 | 516 | 471 | - | - | - |
| Sanasa Development Bank PLC | 18,152 | 1,828 | 1,849 | 256 | 27 | 27 |
| Seylan Bank PLC | 137,789 | 13,846 | 12,015 | 135,000 | 13,846 | 12,150 |
| Seylan Bank PLC-Non Voting | 341,439 | 17,845 | 19,121 | 330,000 | 17,845 | 19,470 |
| Softlogic Finance PLC | 60,515 | 3,340 | 2,203 | 60,515 | 3,340 | 2,058 |
| The Finance Company PLC | 200,000 | 973 | 440 | 200,000 | 973 | 580 |
| Union Bank of Colombo PLC | - | - | - | 10,000 | 170 | 154 |
| | | 131,869 | 102,637 | | 146,853 | 114,369 |
| Beverages, Food and Tobacco | | | | | | |
| Bairaha Farms PLC | 25,000 | 3,962 | 3,683 | - | - | - |
| HVA Foods PLC | 25,000 | 155 | 153 | - | - | - |
| Keells Food Products PLC | 27,672 | 4,746 | 3,874 | 27,672 | 4,746 | 4,372 |
| Lion Brewery Ceylon PLC | 672 | 370 | 363 | - | - | - |
| Lucky Lanka Milk Processing Company PLC | 2,657,487 | 15,808 | 5,049 | 2,657,487 | 15,808 | 8,504 |
| Renuka Agri Foods PLC | 752,274 | 3,091 | 1,956 | 752,274 | 3,091 | 2,182 |
| | | 28,132 | 15,078 | | 23,645 | 15,058 |
| Chemical & Pharmaceuticals | | | | | | |
| CIC Holdings PLC | 2,000 | 144 | 124 | - | - | - |
| CIC Holdings PLC-Non Voting | 25,164 | 1,483 | 1,193 | 7,500 | 585 | 510 |
| | | 1,627 | 1,317 | | 585 | 510 |
| Construction and Engineering | | | | | | |
| Colombo Dockyard PLC | - | - | - | 17,918 | 3,537 | 1,408 |
| MTD Walkers PLC | 130,000 | 7,745 | 3,003 | 130,000 | 7,745 | 5,330 |
| | | 7,745 | 3,003 | | 11,282 | 6,738 |
| Diversified | | | | | | |
| Dunamis Capital PLC | 27,500 | 719 | 644 | - | - | - |
| Taprobane Holdings PLC | 30,000 | 180 | 165 | - | - | - |
| | | 899 | 809 | | - | - |

Notes to the Financial Statements

20 Financial Investments - Held-for-Trading (Contd.)

| | 2017 | | | 2016 | | |
|--------------------------------------|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Diversified Holdings | | | | | | |
| Aitken Spence PLC | 110,000 | 11,110 | 6,006 | 115,000 | 11,616 | 7,475 |
| Browns Investments PLC | 750,000 | 2,475 | 1,950 | - | - | - |
| Hayleys PLC | 500 | 142 | 121 | - | - | - |
| John Keells Holdings PLC | 36,371 | 5,519 | 5,402 | 285,998 | 46,170 | 41,470 |
| Melstacorp PLC | 5,000 | 305 | 298 | 600,000 | 28,973 | 35,580 |
| Sunshine Holdings PLC | 35,211 | 2,119 | 2,007 | - | - | - |
| The Colombo Fort Land & Building PLC | 44,799 | 1,224 | 851 | 45,000 | 1,230 | 900 |
| Vallibel One PLC | 50,000 | 950 | 885 | - | - | - |
| | | 23,844 | 17,520 | | 87,989 | 85,425 |
| Footwear & Textiles | | | | | | |
| Hayleys Fabric PLC | 100,000 | 1,700 | 1,350 | - | - | - |
| Ceylon Leather Products PLC | 8,000 | 615 | 483 | 11,348 | 873 | 794 |
| | | 2,315 | 1,833 | | 873 | 794 |
| Health Care | | | | | | |
| Ceylon Hospitals PLC (Durdans) | 5,000 | 500 | 415 | - | - | - |
| | | 500 | 415 | | - | - |
| Hotels and Travel | | | | | | |
| Aitken Spence Hotel Holdings PLC | 63,219 | 5,779 | 1,865 | 63,219 | 5,793 | 2,725 |
| Asian Hotels & Properties PLC | - | - | - | 132,817 | 9,938 | 7,571 |
| Beruwala Resorts PLC | 100,000 | 100 | 80 | - | - | - |
| Ceylon Hotels Corporation PLC | - | - | - | 2,930 | 75 | 59 |
| Eden Hotel Lanka PLC | 127,743 | 3,676 | 1,813 | 127,743 | 3,677 | 1,725 |
| Galadari Hotels (Lanka) PLC | - | - | - | 20,000 | 292 | 214 |
| John Keells Hotels PLC | 75,000 | 1,175 | 660 | 75,000 | 1,175 | 818 |
| Marawila Resorts PLC | - | - | - | 959,168 | 4,606 | 2,302 |
| Palm Garden Hotels PLC | 147,472 | 10,890 | 3,849 | 147,472 | 10,928 | 4,173 |
| The Kingsbury PLC | 1,937,727 | 41,834 | 26,159 | 1,937,727 | 41,846 | 29,454 |
| Waskaduwa Beach Resort PLC | 50,000 | 245 | 190 | 50,000 | 306 | 220 |
| | | 63,699 | 34,616 | | 78,636 | 49,261 |
| Information and Technology | | | | | | |
| E-Channelling PLC | 15,000 | 120 | 89 | - | - | - |
| | | 120 | 89 | | - | - |

| | 2017 | | | 2016 | | |
|--|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Investment Trust | | | | | | |
| Ceylon Investment PLC | 65,727 | 6,411 | 2,938 | 91,164 | 8,893 | 4,475 |
| Guardian Capital Partners PLC | 18,472 | 1,006 | 556 | 18,472 | 1,006 | 719 |
| Lanka Century Investments PLC | 500,000 | 6,891 | 6,050 | 520,000 | 7,167 | 6,136 |
| Renuka Holdings PLC | - | - | - | 106,441 | 4,266 | 2,246 |
| | | 14,308 | 9,544 | | 21,332 | 13,576 |
| Land and Property | | | | | | |
| Cargo Boat Development Company PLC | 9,984 | 899 | 839 | - | - | - |
| Colombo Land & Development Company PLC | 2,700 | 96 | 53 | 2,700 | 96 | 73 |
| Commercial Development Company PLC | 4,649 | 451 | 325 | 4,649 | 451 | 349 |
| East West Properties PLC | 8,000 | 120 | 90 | - | - | - |
| R I L Property PLC | 25,000 | 200 | 180 | - | - | - |
| Seylan Developments PLC | 75,000 | 1,125 | 1,020 | - | - | - |
| | | 2,891 | 2,507 | | 547 | 422 |
| Manufacturing | | | | | | |
| Abans Electricals PLC | 5,000 | 521 | 422 | - | - | - |
| ACL Cables PLC | 50,000 | 2,755 | 2,120 | - | - | - |
| ACME Printing & Packaging PLC | - | - | - | 131,023 | 1,137 | 812 |
| Alufab PLC | 60,000 | 1,660 | 1,380 | - | - | - |
| Central Industries PLC | - | - | - | 5,000 | 250 | 248 |
| Ceylon Grain Elevators PLC | 60,000 | 4,186 | 3,966 | - | - | - |
| Chevron Lubricants Lanka PLC | 35,000 | 4,656 | 4,165 | - | - | - |
| Dankotuwa Porcelain PLC | - | - | - | 630,902 | 6,301 | 4,479 |
| Kelani Tyres PLC | 115,000 | 9,023 | 5,106 | 115,000 | 9,023 | 7,464 |
| Lanka Tiles PLC | - | - | - | 48,253 | 5,786 | 4,627 |
| Pelwatte Sugar Industries PLC | 68,400 | 2,925 | 978 | 68,400 | 2,925 | 978 |
| Piramal Glass Ceylon PLC | - | - | - | 800,000 | 5,100 | 4,240 |
| Richard Pieris Exports PLC | 2,000 | 470 | 354 | - | - | - |
| Royal Ceramics Lanka PLC | 68,323 | 8,740 | 7,823 | - | - | - |
| Sierra Cables PLC | 1,390,000 | 6,157 | 3,475 | 1,390,000 | 6,157 | 4,587 |
| Teejay Lanka PLC | 75,000 | 2,775 | 2,550 | - | - | - |
| | | 43,868 | 32,339 | | 36,679 | 27,435 |
| Motors | | | | | | |
| United Motors Lanka PLC | 25,000 | 2,025 | 1,950 | - | - | - |
| | | 2,025 | 1,950 | | - | - |

Notes to the Financial Statements

20 Financial Investments - Held-for-Trading (Contd.)

| | 2017 | | | 2016 | | |
|--|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| Plantation | | | | | | |
| Balangoda Plantations PLC | - | - | - | 497,486 | 14,996 | 6,069 |
| Elpitiya Plantations PLC | 50,000 | 1,497 | 1,410 | - | - | - |
| Kotagala Plantations PLC | - | - | - | 67,444 | 2,644 | 600 |
| | | 1,497 | 1,410 | | 17,640 | 6,669 |
| Power and Energy | | | | | | |
| Laugfs Gas PLC | 75,000 | 1,963 | 1,762 | 26,088 | 1,008 | 858 |
| Laugfs Gas PLC-Non Voting | 25,000 | 966 | 500 | - | - | - |
| Resus Energy PLC | 173,037 | 3,414 | 3,149 | 172,737 | 3,407 | 3,852 |
| Vallibel Power Erathna PLC | 125,000 | 975 | 937 | 50,000 | 459 | 440 |
| | | 7,318 | 6,348 | | 4,874 | 5,150 |
| Service | | | | | | |
| Ceylon Tea Brokers PLC | 114,778 | 557 | 494 | 192,655 | 937 | 751 |
| Renuka Capital PLC | 63,500 | 460 | 286 | 135 | 172 | 109 |
| | | 1,017 | 780 | | 1,109 | 860 |
| Telecommunication | | | | | | |
| Dialog Axiata PLC | - | - | - | 100,000 | 1,149 | 1,050 |
| | | - | - | | 1,149 | 1,050 |
| Trading | | | | | | |
| Brown & Company PLC | 19,061 | 1,610 | 1,344 | 5,178 | 526 | 435 |
| Eastern Merchants PLC | - | - | - | 257,922 | 2,179 | 1,599 |
| Tess Agro PLC-Non Voting | 100,000 | 130 | 100 | - | - | - |
| | | 1,740 | 1,444 | | 2,705 | 2,034 |
| Total value of quoted equities and unit trusts | | 335,414 | 233,639 | | 435,898 | 329,351 |
| 20.2 Other Debt Securities | | | | | | |
| Commercial Credit & Finance PLC | 20,000 | 2,141 | 2,325 | 20,000 | 2,141 | 2,235 |
| Hatton National Bank PLC | 26,000 | 2,377 | 2,288 | - | - | - |
| Total value of listed debentures | | 4,518 | 4,613 | | 2,141 | 2,235 |
| Total value of financial assets at fair value through profit or loss | | 339,932 | 238,252 | | 438,039 | 331,586 |
| Marked to market valuation loss | | [101,680] | | | [106,453] | |
| Fair value of financial assets designated at fair value through profit or loss | | 238,252 | | | 331,586 | |

21 Loans & Receivables to Customers

Accounting Policy

Financial assets classified as loans and receivables include non-derivative financial assets with fixed or determinable payments that are not quoted in active market, other than:

- Those that the Company and the Group intends to sell immediately or in the near term, and those that upon initial recognition designates as at fair value through profit or loss.
- Those that the Company and the Group upon initial recognition designates at available-for-sale.
- Those for which the Company and the Group may not recover substantially all of its initial investment because of credit deterioration.

After initial measurement, loans and receivables are subsequently measured at amortised cost using EIR, less allowances for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortisation is included in 'Interest income' in the Statement of Profit or Loss. The losses arising from impairment are recognised in the Statement of Profit or Loss 'Impairment charges for loans and receivables and other losses'.

Lease and Hire Purchase Receivables

The determination of whether an arrangement is a lease, or it contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Group/Company as a Lessor

Leases, where the Group/Company does not transfer substantially all of the risk and benefits of ownership of assets are classified as operating leases. Initial direct cost incurred in negotiating operating leases are added to the carrying amount of the leased assets and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

Group as a Lessee

Leases that do not transfer to the Group/Company substantially all the risk and benefits incidental to ownership of the leased items are operating leases. Operating lease payments are recognised as an expense in the Statement of Profit or Loss on a straight-line basis over the lease term. Contingent rental payable is recognised as an expense in the period in which they are incurred.

'Day 1' Profit or Loss

Staff loans granted at below market interest rates are recognised at fair value. The difference between the fair value and the amount disbursed were treated as 'day 1' difference and amortised as staff cost over the loan period by using effective interest rate (EIR). The staff loans subsequently measured at amortised costs.

Impairment of Financial Assets

The Group assesses at each reporting date to ascertain, whether there is any objective evidence that a financial asset is impaired. A financial asset is deemed to be impaired if, and only if, there is an objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (an incurred loss events) and that loss event (or event) has an impact on the estimated future cash flows of the financial assets that can be reliably estimated.

Notes to the Financial Statements

21 Loans and Receivables to Customers (Contd.)

Loans and Receivables

Losses for impaired loans and receivables are recognised promptly when an objective evidence has occurred. Impairment allowances are calculated on individual and collective basis. Impairment losses are recorded as charges to the Statement of Profit or Loss. The carrying amount of impaired loans and receivables on the Statement of Financial Position is reduced through the use of impairment allowance accounts. Losses expected from future events are not recognised.

Individually Assessed Loans and Receivables

For all loans and receivables that are considered individually significant, the Company assesses on a case by case basis at each reporting date to ascertain whether there is any objective evidence that a loan is impaired. The criteria used to determine that there is such objective evidence include;

- Known cash flow difficulties experienced by the borrower;
- Past due contractual payments of either principal or interest;
- The probability that the borrower will enter bankruptcy or other financial realisation; and
- A significant downgrading in credit rating by an external credit rating agency.

For those loans and receivables where objective evidence of impairment exists, impairment losses are determined considering the following factors:

- Company's aggregate exposure to the customer;
- The viability of the customer's business model and their capacity to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
- The amount and timing of expected receipts and recoveries;
- The realisable value of security (or other credit mitigates) and likelihood of successful re-possession;
- The likely deduction of any costs involved in recovery of amounts outstanding.

Impairment losses are calculated by discounting the expected future cash flows of loans and receivables at its original effective interest rate and comparing the resultant present value with loans and receivables in current carrying amount. The impairment allowances on individually significant accounts are reviewed more regularly when circumstances require. This normally encompasses re-assessment of the enforceability of any collateral held and the timing and amount of actual and anticipated receipts. Individually assessed impairment allowances are only released when there is reasonable and objective evidence of a reduction in the established loss estimate.

Collectively Assessed Loans and Receivables

Impairment is assessed on a collective basis to cover losses which have been incurred but have not yet been identified on loans and receivables subject to individual's assessment.

Incurred-But-Not-Yet Identified Impairment

Individually assessed loans and receivables for which no evidence of loss has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for the purpose of calculating an estimated collective loss. This reflects impairment losses that the Group has incurred as a result of events occurring before the reporting date, which the Company and the Group are not able to identify on an individual loan basis and that can be reliably estimated. These losses will

only be individually identified in the future. As soon as information becomes available which identifies losses on individual loans and receivables within the Group, those loans and receivables are removed from the Group and assessed on an individual basis for impairment.

The collective impairment allowance is determined after taking into account;

- Historical loss experience in portfolios of similar credit risk ; and
- Management's experienced judgment as to whether current economic and credit conditions are such that the actual level of inherent losses at the reporting date is likely to be greater or less than that suggested by historical experience.

Loans and receivables are grouped into ranges according to the number of days in arrears and statistical analysis is used to estimate the likelihood that loans and receivables in each range will progress through the various stages of delinquency and ultimately prove irrecoverable.

Current economic conditions and portfolio risk factors are also evaluated when calculating the appropriate level of allowance required to cover the inherent loss. These additional macro and portfolio risk factors may include:

- Recent lending portfolio growth and product mix.
- Exchange rates, interest rates.
- Changes in laws and regulations.

Reversals of Impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related to the objective of an event occurring after the impairment it is recognised, the excess will be written back by reducing the loan impairment allowance account accordingly. The write-back is recognised in the Statement of Profit or Loss.

Write-off of Loans and Receivables

Loans and receivables (and the related impairment allowance accounts) are normally written off, either partially or in fully, when there is no realistic prospect of recovery. Where loans and receivables are secured, this is generally after receipt of any proceeds from the realisation of security.

Re-negotiated Loans and Receivables

Where possible, the Group/Company seeks to re-structure loans and receivables rather than to take possession of collateral. This may involve extending the payment arrangements and the agreements of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original EIR as calculated before the modification of terms and the loan is no longer considered past due. The management continuously reviews the re-negotiated loans and receivables to ensure that all criteria are met and that future payments are likely to occur. The loans and receivables continue to be subject to any criteria are met and that future payments are likely to occur. The loans and receivables continue to be subjected to an individual or collective impairment assessment calculated using the original EIR.

Notes to the Financial Statements

21 Loans & Receivables to Customers (Contd.)

21.1 Bills receivable

| As at 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Bills discounted | 628,505 | 874,045 | 628,505 | 874,045 |
| | 628,505 | 874,045 | 628,505 | 874,045 |
| Less: Allowance for impairment losses [Note 21.1.1] | 134,409 | 134,642 | 134,409 | 134,642 |
| | 494,096 | 739,403 | 494,096 | 739,403 |

21.1.1 Movement in Allowance for Individual and Collective Impairment During the Year

Individual Impairment Charges

| | | | | |
|--|---------|----------|---------|----------|
| As at 01 January | 122,874 | 121,056 | 122,874 | 121,056 |
| Charge / (write back) to Statement of Profit or Loss | (208) | 15,818 | (208) | 15,818 |
| Write off during the year | - | (14,000) | - | (14,000) |
| As at 31 December | 122,666 | 122,874 | 122,666 | 122,874 |

Collective Impairment Charges

| | | | | |
|--|---------|---------|---------|---------|
| As at 01 January | 11,768 | 11,568 | 11,768 | 11,568 |
| Charge / (write back) to Statement of Profit or Loss | (25) | 200 | (25) | 200 |
| As at 31 December | 11,743 | 11,768 | 11,743 | 11,768 |
| Total | 134,409 | 134,642 | 134,409 | 134,642 |

21.2 Loans and Advances to Customers

| | | | | |
|---|------------|------------|------------|------------|
| Term loans | 5,420,809 | 5,049,631 | 5,343,358 | 5,049,631 |
| Personal loans | 5,322,838 | 4,681,342 | 5,322,838 | 4,681,342 |
| Cheque discounting | 29,149 | 34,314 | 29,149 | 34,314 |
| Staff loans | 261,188 | 213,491 | 261,188 | 213,491 |
| Margin trading | 123,112 | 122,149 | 123,112 | 122,149 |
| Micro finance | 1,040,888 | 993,172 | 1,040,888 | 993,172 |
| Commercial papers and other placements | - | - | 67,077 | 67,024 |
| Pawning | 699,634 | 499,855 | 699,634 | 499,855 |
| Real estate loans | 30,778 | 37,036 | 30,778 | 37,036 |
| Loans to life policy holders | - | - | 5,197 | 4,622 |
| Loans against fixed deposits | 418,409 | 308,494 | 418,409 | 308,494 |
| | 13,346,805 | 11,939,484 | 13,341,628 | 12,011,130 |
| Less: Allowance for impairment losses [Note 21.2.1] | 748,672 | 618,639 | 748,672 | 618,639 |
| Net loans and advances to customers | 12,598,133 | 11,320,845 | 12,592,956 | 11,392,491 |

21.2.1 Movement in Allowance for Individual and Collective Impairment During the Year

| As at 31 December | Company | | Group | |
|--|-------------------|-------------------|-------------------|-------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Individual Impairment Charges | | | | |
| As at 01 January | 403,512 | 413,391 | 403,512 | 413,391 |
| Charge / [write back] to Statement of Profit or Loss | [16,811] | 36,685 | [16,811] | 36,685 |
| Write off during the year | - | [46,564] | - | [46,564] |
| As at 31 December | 386,701 | 403,512 | 386,701 | 403,512 |
| Collective Impairment Charges | | | | |
| As at 01 January | 215,127 | 267,424 | 215,127 | 267,424 |
| Charge / [write back] to Statement of Profit or Loss | 146,844 | [52,297] | 146,844 | [52,297] |
| As at 31 December | 361,971 | 215,127 | 361,971 | 215,127 |
| Total | 748,672 | 618,639 | 748,672 | 618,639 |
| 21.3 Lease and Hire Purchase Receivable | | | | |
| 21.3.a Finance Lease / Hire Purchase Receivable within One Year from the Reporting Date | | | | |
| Total lease and hire purchase rental receivable | 20,535,637 | 19,177,170 | 20,535,637 | 19,177,170 |
| Less: Lease and hire purchase rental receivable after one year | 11,909,806 | 12,539,828 | 11,909,806 | 12,539,828 |
| Lease rental receivable within one year from the reporting date | 8,625,831 | 6,637,342 | 8,625,831 | 6,637,342 |
| Less : unearned lease and hire purchase income | 2,135,846 | 1,931,241 | 2,135,846 | 1,931,241 |
| | 6,489,985 | 4,706,101 | 6,489,985 | 4,706,101 |
| 21.3.b Finance Lease / Hire Purchase Receivable after One Year from the Reporting Date | | | | |
| Lease and hire purchase rental receivable after one year from the reporting date | 11,909,806 | 12,539,828 | 11,909,806 | 12,539,828 |
| Less : Unearned lease and hire purchase income | 2,310,884 | 1,930,532 | 2,310,884 | 1,930,532 |
| | 9,598,922 | 10,609,296 | 9,598,922 | 10,609,296 |
| | 16,088,907 | 15,315,397 | 16,088,907 | 15,315,397 |
| Less : Provision for impairment [Note 21.3.c] | 427,475 | 323,646 | 427,475 | 323,646 |
| Net investment in leases and hire purchase | 15,661,432 | 14,991,751 | 15,661,432 | 14,991,751 |

Notes to the Financial Statements

21 Loans & Receivables to Customers (Contd.)

21.2.1 Movement in Allowance for Individual and Collective Impairment During the Year

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| 21.3.c Movement in Allowance for Individual and Collective Impairment During the Year | | | | |
| Individual Impairment Charges | | | | |
| As at 01 January | 158,654 | 513,515 | 158,654 | 513,515 |
| Charge /(write back) to Statement of Profit or Loss | 61,848 | 29,884 | 61,848 | 29,884 |
| Write off during the year | [10,602] | [384,745] | [10,602] | [384,745] |
| As at 31 December | 209,900 | 158,654 | 209,900 | 158,654 |
| Collective Impairment Charges | | | | |
| As at 01 January | 164,992 | 171,043 | 164,992 | 171,043 |
| Charge /(write back) to Statement of Profit or Loss | 52,583 | [6,051] | 52,583 | [6,051] |
| As at 31 December | 217,575 | 164,992 | 217,575 | 164,992 |
| Total | 427,475 | 323,646 | 427,475 | 323,646 |

22 Financial Investments - Available-for-Sale

Accounting Policy

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for-sale are those which are neither classified as held-for-trading nor designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

After initial measurement, available-for-sale financial investments are subsequently measured at fair value.

Unrealized gains and losses are recognised directly in equity (Other Comprehensive Income) in the 'available-for-sale reserve'. When the investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the Statement of Profit or Loss in 'other operating income'. Interest earned whilst holding available-for-sale financial investments is reported as 'interest income' using the EIR.

Dividends earned, whilst holding available-for-sale financial investments are recognised in the Statement of Profit or Loss as 'net trading income', when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the Statement of Profit or Loss in 'Impairment losses on financial investments' and removed from the 'Available-for-sale reserve'.

Impairment of Available-for-Sale Financial Assets

For available-for-sale financial investments, the Group assesses at each reporting date to ascertain whether there is objective evidence that an investment is impaired. In the case of debt instruments classified as available-for-sale, the Group assesses individually as to whether there is objective evidence of impairment based on the same criteria as financial assets carried at amortised cost.

However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the Statement of Profit or Loss. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of 'Interest and similar income'. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognised in the Statement of Profit or Loss, the impairment loss is reversed through the Statement of Profit or Loss.

Impairment of Available-for-Sale-Investment

The Group and the Company review their financial assets classified as available-for-sale at each reporting date to assess whether they are impaired. This requires similar judgments as applied to the individual assessment of loans and receivables.

In the case of equity investments classified as available-for-sale, objective evidence would also include a significant or prolonged decline in the fair value of the investment below its cost. The determination of what is significant or prolonged requires judgment. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the Statement of Other Comprehensive Income is removed from equity and recognised in the Statement of Profit or Loss. Impairment losses on equity investments are not reversed through the Statement of Profit or Loss; increase in the fair value after impairment are recognised in the Statement of Other Comprehensive Income.

| As at 31 December | Company | | Group | |
|---|------------------|------------------|------------------|------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Government securities (Note 22.1) | 640,791 | 2,694,335 | 978,638 | 3,049,945 |
| Unquoted investments (Note 22.2) | 51,554 | 41,310 | 51,554 | 42,287 |
| Unit Trust | 1,122,836 | - | 1,161,650 | 34,583 |
| Total financial investments - Available-for-sale | 1,815,181 | 2,735,645 | 2,191,842 | 3,126,815 |
| 22.1 Government Securities | | | | |
| Treasury bills | 191,820 | 2,277,121 | 191,820 | 2,320,870 |
| Treasury bonds | 448,971 | 417,214 | 786,818 | 729,075 |
| | 640,791 | 2,694,335 | 978,638 | 3,049,945 |

Notes to the Financial Statements

22 Financial Investments - Available-for-Sale (Contd.)

| As at 31 December | Holding % | 2017 | | | 2016 | | |
|--|-----------|--------------|-----------------------|-----------------------|--------------|-----------------------|-----------------------|
| | | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 | No of Shares | Total Cost Rs.'000 | Fair Value Rs.'000 |
| 22.2 Unquoted Investments | | | | | | | |
| Company | | | | | | | |
| Mega Containers Limited | 6.21 | 1,000,000 | 10,000 | 23,794 | 1,000,000 | 10,000 | 20,491 |
| Ceylinco Investment Company Limited [Note 22.2.1] | 46.35 | 500,000 | 5,000 | - | 500,000 | 5,000 | - |
| Credit Information Bureau of Sri Lanka Limited | 0.22 | 540 | 54 | 54 | 540 | 54 | 54 |
| Ranwan Industries (Private) Limited | 5.00 | 165,790 | 3,600 | - | 165,790 | 3,600 | - |
| LVL Energy Fund Limited | 0.43 | 2,500,000 | 20,000 | 26,500 | 2,500,000 | 20,000 | 20,000 |
| Finance & Guarantee Company Limited | 0.15 | 2,506,562 | 17,546 | 1,206 | 2,506,562 | 17,546 | 765 |
| San Michele Limited | - | 50,000 | 500 | - | 50,000 | 500 | - |
| | | | 56,700 | 51,554 | | 56,700 | 41,310 |
| Adjustment for fair value changes | | | 16,500 | | | [11,290] | |
| Adjustment due to impairment | | | [21,646] | | | [4,100] | |
| Total Unquoted Investments | | | 51,554 | | | 41,310 | |
| Group | | | | | | | |
| Mega Containers Limited | 6.21 | 1,000,000 | 10,000 | 23,794 | 1,000,000 | 10,000 | 20,491 |
| Ceylinco Investment Company Limited | 46.35 | 500,000 | 5,000 | - | 500,000 | 5,000 | - |
| Credit Information Bureau of Sri Lanka Limited | 0.22 | 540 | 54 | 54 | 540 | 54 | 54 |
| Ranwan Industries (Private) Limited | 5.00 | 165,790 | 3,600 | - | 165,790 | 3,600 | - |
| LVL Energy Fund Limited | 0.43 | 2,500,000 | 20,000 | 26,500 | 2,500,000 | 20,000 | 20,000 |
| Finance & Guarantee Company Limited | 0.15 | 2,506,562 | 17,546 | 1,206 | 2,506,562 | 17,546 | 765 |
| San Michele Limited | - | 50,000 | 500 | - | 50,000 | 500 | - |
| Equity One Limited | - | 26,664 | - | - | 26,664 | 977 | 977 |
| | | | 56,700 | 51,554 | | 57,677 | 42,287 |
| Adjustment for fair value changes | | | 16,500 | | | [11,290] | |
| Adjustment due to impairment | | | [21,646] | | | [4,100] | |
| Total Unquoted Investments | | | 51,554 | | | 42,287 | |

22.2.1 Although the Company has acquired 46.35% equity capital of Ceylinco Investment Company Limited, the investment has not been classified as an associate company due to pending court decision on the ownership structure of the Company.

23 Financial Investments - Held-to-Maturity

Accounting Policy

Held-to-Maturity financial investments are non-derivative financial assets with fixed or determinable payments and fixed maturity dates, which the Group has the positive intention and ability to hold to maturity. Subsequent to initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method less any impairment. Amortised cost is calculated by taking in to accounting any discount or premium on acquisition and fees that are an integral part of the EIR. The amortisation is included in 'interest income' in the Statement of Profit or Loss. The losses arising from impairment of such investments are recognised in the Statement of Profit or Loss in 'impairment charges for loans and other losses'.

If the Group were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than in certain specific circumstances permitted in the Sri Lanka Accounting Standard-LKAS 39-'Financial Instruments: Recognition and Measurement') the entire category would be tainted and would have to be re-classified as available-for-sale. Furthermore, the Group would be prohibited from classifying any financial asset as held-to-maturity during the following two years.

Impairment of Held-to-Maturity Financial Assets

An impairment loss in respect of held-to-maturity financial assets measured at amorised cost is calculated as the difference between its carrying amount and the present value of estimated future cash flows discounted at the asset's original EIR and is recognised in the Statement of Profit or Loss. Interest on impaired assets continues to be recognised through the unwinding of discount. When a subsequent event caused the amount of impairment loss to decrease, the decrease in impairment loss is reversed through the Statement of Profit or Loss.

| As at 31 December | Company | | Group | |
|----------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Debt securities - Treasury bonds | 479,362 | 57,766 | 479,362 | 57,766 |
| | 479,362 | 57,766 | 479,362 | 57,766 |

24 Investment in Associate Company

Accounting Policy

Investment in associate is accounted for at cost in the Company's Financial Statements and under the equity method in the Consolidated Financial Statements.

Under the equity method, the investment in associate is initially accounted for at cost and the carrying amount is adjusted for post-acquisition changes in the Company's share of net assets of the associate, less any impairment in the Company's net investment in associate.

Associate is an entity in which the Company has significant influence, but no control over the financial and operating policies.

Investment in Associate is accounted for using the equity method and is recognised initially at cost in terms of the Sri Lanka Accounting Standard - LKAS 28 - 'Investment in Associates and Joint Ventures'. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised but it subjected to impairment test. The Company's investments include goodwill identified on acquisition, net of any accumulated impairment losses.

Notes to the Financial Statements

24 Investment in Associate Company [Contd.]

The Consolidated Financial Statements include the Company's share of the income and expenses and equity movements of the associate, after adjustments being made to align the accounting policies with those of the Group from the date that significant influence effectively commences until the date that significant influence effectively ceases.

When the Company's share of losses exceeds its interest in the associate, the carrying amount of that interest is reduced to nil and the recognition of further losses is discontinued except to the extent that the Company has an obligation or made payments on behalf of the associate. If the associate subsequently reports profits, the Company resumes recognising its share of those profits only after its share of the profits equals the share of losses not recognised.

Profit and losses resulting from transactions between the Company and the associate are eliminated to the extent of the interest in the associate. The Company discontinues the use of the equity method from the date that it ceases to have significant influence over an associate and accounts for the investment cost in accordance with the Sri Lanka Accounting Standard - LKAS 39 - 'Financial Instruments: Recognition and Measurement'.

| As at 31 December | Country of Incorporation | Principal Activity | No. of Shares | Holding % | Company | | | |
|----------------------------------|--------------------------|--------------------|---------------|-----------|-----------------|---------------------------------|-----------------|---------------------------------|
| | | | | | 2017 | | 2016 | |
| | | | | | Cost Rs.'000 | Directors' Valuation Rs.'000 | Cost Rs.'000 | Directors' Valuation Rs.'000 |
| Unquoted | | | | | | | | |
| Lanka Securities (Pvt) Ltd | Sri Lanka | Share Brokering | 5,212,543 | 29.00 | 81,084 | 81,084 | 81,084 | 81,084 |
| Balance as at 31 December | | | | | 81,084 | 81,084 | 81,084 | 81,084 |

24.1 Carrying Value on Equity Basis

| As at 31 December | Group | |
|--|----------------------------|-----------------|
| | Lanka Securities (Pvt) Ltd | |
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Net assets at the beginning of the year | 91,325 | 96,485 |
| Add : Profit / (loss) before tax accruing to the group | 1,059 | [5,437] |
| Less : Income tax | [1,170] | [758] |
| Add : Other comprehensive income for the year | 1,239 | 1,035 |
| Net assets at the end of the year | 92,453 | 91,325 |

24.2 Summarized Financial Information of Associate

| For the year ended 31 December | Lanka Securities (Pvt) Ltd | |
|---|----------------------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Income | 121,063 | 89,605 |
| Less : Expenses | 117,412 | 108,354 |
| Profit/[loss] before taxation | 3,651 | [18,749] |
| Less : Income tax expense /[reversal] | 4,035 | 2,609 |
| Loss for the year | [384] | [21,358] |
| Other comprehensive income/[expenses] | 4,274 | 3,569 |
| Total comprehensive income/[expenses] for the year | 3,890 | [17,789] |
| As at 31 December | 2017 Rs.'000 | 2016 Rs.'000 |
| Total assets | 615,546 | 391,590 |
| Total liabilities | 296,743 | 76,677 |

25 Investment in Subsidiary

Accounting Policy

Investment in subsidiaries are stated at cost, net of any impairment losses which are charged to the Statement of Profit or Loss and it is in accordance with the Sri Lanka Accounting Standards-LKAS 27- 'Separate Financial Statements'.

Subsidiaries are entities that are controlled by the Company/Group. Subsidiaries are consolidated from the date on which control is transferred to the Company and continue to be consolidated until the date when such control ceases. The Company is presumed to control an investee when it is exposed, or has right, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

Intra-group balances and transactions, income, expenses and any unrealised gains arising from intra-group transactions are eliminated in full in preparing the Consolidated Financial Statements.

Non-controlling interests represent the portion of profit or loss and net assets of subsidiaries not owned, directly or indirectly, by the Company.

Non-controlling interests are presented separately in the Consolidated Statement of Profit or Loss and within equity in the consolidated Statement of Financial Position but separate from parent shareholder's equity. Any losses applicable to the non-controlling interests are allocated against the interests of the non-controlling interest even if this result in a defect balance. Acquisition of non-controlling interests are accounted for using the parent entity extension method, whereby the difference between the consideration and the fair value of the share of the net assets acquired is recognised as equity.

Notes to the Financial Statements

25 Investment in Subsidiary (Contd.)

| As at 31 December | | | 2017 | | 2017 | | 2016 | |
|--|--------------------------|--------------------|---------------|-----------|-----------------|---------------------------------|-----------------|---------------------------------|
| | Country of Incorporation | Principal Activity | No. of Shares | Holding % | Cost Rs.'000 | Directors' Valuation Rs.'000 | Cost Rs.'000 | Directors' Valuation Rs.'000 |
| Unquoted | | | | | | | | |
| MBSL Insurance Company Ltd (Note 25.1) | Sri Lanka | Insurance | 475,697,403 | 84.12 | 516,096 | 21,117 | 516,096 | 77,306 |
| | | | 475,697,403 | | 516,096 | 21,117 | 516,096 | 77,306 |
| Less : Impairment provision (Note 25.2) | | | | | [494,979] | | [438,790] | |
| Carrying value at 31 December | | | | | 21,117 | | 77,306 | |

25.1 Summarised Financial Information of MBSL Insurance Company Ltd.

| For the year ended 31 December | 2017 Rs.'000 | 2016 Rs.'000 |
|---|------------------|------------------|
| Net operating income | 308,752 | 296,067 |
| Less : Operating expenses | 355,188 | 516,591 |
| Loss before income tax | [46,436] | [220,524] |
| Less : Income tax expense / [reversal] | 7,143 | 10,655 |
| Loss for the year | [53,579] | [231,179] |
| Other comprehensive income/(expenses) | 8,256 | [10,204] |
| Total comprehensive income/(expenses) for the year, net of tax | [45,323] | [241,383] |
| As at 31 December | 2017 Rs.'000 | 2016 Rs.'000 |
| Loans and receivables | 512,930 | 675,495 |
| Reinsurance assets-insurance contracts | 283,083 | 289,794 |
| Insurance receivables | 12,254 | 211,672 |
| Property and equipment & intangible assets | 43,966 | 63,077 |
| Other assets | 505,264 | 534,732 |
| Total assets | 1,357,498 | 1,774,770 |
| Due to banks | 6,028 | 23,364 |
| Insurance contract liabilities | 977,119 | 1,295,292 |
| Insurance payables | 50,390 | 68,673 |
| Other liabilities | 298,822 | 295,293 |
| Total liabilities | 1,332,359 | 1,682,622 |
| Total equity | 25,139 | 92,148 |
| Total liabilities and equity | 1,357,498 | 1,774,770 |

25.2 Impairment Provision

At the end of the reporting period, the Company assessed the recoverable amount of the investment in subsidiary, MBSL Insurance Company Limited of Rs. 516.1 Mn and the recoverable amount of the goodwill of Rs.18.2 Mn respectively.

The recoverable amount of investment in subsidiary as at 31 December 2017 was determined as Rs.21.1 Mn and further, impairment allowance of Rs.56.1 Mn [2016: Rs.232.9 Mn] was made during the year 2017 in the Company's Financial Statements.

Impairment of Investment in Subsidiary :

The main indicator that was considered for the assessment of impairment of the investment in subsidiary was the continuous losses in the current and previous years resulting in the carrying value of the investment in the Company's Financial Statements exceeding the subsidiary's net assets.

The recoverable amount of the investment in subsidiary was assessed using the net asset based valuation. The net asset of the Company comprises of life insurance fund reserve and net equity. The management decided to use net asset-based approach by considering the current status of the Subsidiary as a most suitable approach to compare with other competitors.

The value in use model was not considered for the purpose of determination of the recoverable value of the investment since the management has decided to find an investor for a significant minority. For this purpose Expression of Interest has been called by MBSL Insurance Company Limited [MBSLI] and in the process of find a prospective investor to invest Rs. 700 Mn for a significant minority stake in MBSLI. As the process is not completed, net assets value has been used for impairment computation.

The impairment loss has been separately presented in the Statement of Profit or Loss.

26 Investment Properties

Accounting Policy

Investment properties are properties held either to earn rental income or for capital appreciation or for both. But not for sale in the ordinary course of business, used in the production or supply of goods or service or for administrative purpose.

Basis of Measurement

An investment property is measured initially at its cost. The cost of a purchased investment property comprises of its purchase price and any directly attributable expenditure. The carrying amount includes the cost of replacing part of an existing Investment Property at the time that cost is incurred if the recognition criteria are met and excludes the cost of day-to-day servicing of an Investment Property.

The Group adopts the cost model for subsequent measurement of investment properties in accordance with Sri Lanka Accounting Standard - LKAS 40 - 'Investment Property'. Accordingly, land classified as investment property is stated at cost, and buildings classified as investment property are stated at cost less any accumulated depreciation and any accumulated impairment losses. Provision for depreciation is made over the period of 20 years at the rate of 5% per annum using the straight- line method for buildings classified as investment property. Land is not depreciated.

The Group revalues investment property at least once in five years for disclosure purpose.

Notes to the Financial Statements

26 Investment Properties [Contd.]

Derecognition

Investment Properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. The difference between the net disposal proceeds and the carrying amount of the asset is recognised in the Statement of Profit or Loss in the period of derecognition.

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Cost | | | | |
| Cost as at 01 January | 150,085 | 165,876 | 150,085 | 165,876 |
| Less: Disposals | 991 | 15,791 | 991 | 15,791 |
| Cost as at 31 December | 149,094 | 150,085 | 149,094 | 150,085 |
| Accumulated depreciation as at 31 December | 25,321 | 22,415 | 25,321 | 22,415 |
| Net book value as at 31 December | 123,773 | 127,670 | 123,773 | 127,670 |
| Accumulated depreciation | | | | |
| Balance as at 01 January | 22,415 | 20,036 | 22,415 | 20,036 |
| Charge for the year | 2,906 | 2,961 | 2,906 | 2,961 |
| Less: Disposals | - | 582 | - | 582 |
| Balance as at 31 December | 25,321 | 22,415 | 25,321 | 22,415 |
| Rental income derived from investment property | Nil | Nil | Nil | Nil |
| Direct operating expenses arising from investment property that generated rental income during the year | Nil | Nil | Nil | Nil |
| Direct operating expenses arising from investment property that did not generate rental income during the year | 915 | 902 | 915 | 902 |

26.1 Investment Properties Held by the Company/ Group

As at 31 December

| Location | No of Buildings | Building sq.ft | Extent Perches | Fair Value Hierarchy | Cost / Carrying amount | | | Fair Value | | |
|--|-----------------|----------------|----------------|----------------------|------------------------|-----------|---------|------------|-----------|---------|
| | | | | | Land | Buildings | Total | Land | Buildings | Total |
| | | | | | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| No. 64 & 66, Nonagama Road, Pallegama, Embilipitiya. | - | - | 16.61p | Level 3 | 1,750 | - | 1,750 | 30,000 | N/A | 30,000 |
| No 385/1, Kotte Road, Pitakotte. | 1 | 2,896 | 19.01p | Level 3 | 2,958 | 1,730 | 4,688 | 3,343 | 1,955 | 5,298 |
| No 116/4, 116/7, 116/26, 116/27, 116/29 1st Cross Street, Colombo 11. | - | - | 12.35P | Level 3 | 1,249 | - | 1,249 | 2,602 | N/A | 2,602 |
| No 102 & 104, Dam Street, Colombo 12. (Note.26.1.a) | 1 | 20,368 | 1R-10.7P | Level 3 | 17,970 | 11,989 | 29,959 | 213,000 | 20,000 | 233,000 |
| Kumbuththukuliya watte, Bangadeniya Road, Puttalam. | - | - | 2.0A | Level 3 | 600 | - | 600 | 3,400 | N/A | 3,400 |
| Mirissawelawatta hena; Thekkawatta Dambadeniya | - | - | 1A-OR-28.00P | Level 3 | 162 | - | 162 | 600 | N/A | 600 |
| No 64, Gabadawa Estate, Pitipana, Homagama | - | - | 10.00P | Level 3 | 686 | - | 686 | 1,394 | N/A | 1,394 |
| Fingara town & country Club, no.50/21, Old Kesbewa Road, Boralesgamuwa | 1 | - | 2A-1R-4.35P | Level 3 | 65,604 | 44,396 | 110,000 | 182,175 | 115,840 | 298,015 |
| | | | | | 90,979 | 58,115 | 149,094 | 436,514 | 137,795 | 574,309 |

26.1.a The fair value of the investment properties as at 31 December 2017 was based on market valuations carried out in the year 2013, 2014, 2016 & 2017 by Mr. D N Dhammika Baranage RICS (UK), DIV AIS (SL) and Mr. H A W Perera B.Sc. Estate Mgt & Valuation [Special], Mr. Samantha Kumara Madawan Arachchi Bs.(EMV), City Planning [JP], Dip [UPM] NI, AIREV and Mr. A.G. Gunarathne B.Sc. Estate Mgt & Valuation, F.I.V [Sri Lanka], L.G.T Tungasiri(AIV).F.I.V [Sri Lanka].Dip.in Valuation[S.L.T.C], who are independent valuers not connected with the Company. The Directors have reviewed the values of the investment properties as at 31 December 2017 and concluded that there was no impairment.

26.1.b The Company has entered into an agreement with 71 tenants to sell the lease hold rights of the property at No. 102 & 104, Dam Street, Colombo 12 subject to the approval of Urban Development Authority (UDA). The date of the completion of this sale and the execution of the deed of transfer in favor of the purchaser in respect of lease hold rights of the premises shall be fixed subsequent to the registration of the said premises as a condominium unit and upon a condominium deed of declaration being executed and obtaining all necessary approvals from the UDA for such registration within five years from the execution of said agreement. However, the Company has not obtained the condominium status and other necessary approval from UDA to proceed selling the lease hold right agreement till the reporting date. MBSL shall expeditiously affect the transfer deeds contemplated by the agreement after having obtained the registration of the condominium plan and the condominium declaration and any other statutory approval from UDA and upon the balance payment of the purchase consideration settled in full.

Notes to the Financial Statements

27 Property and Equipment

Accounting Policy

Basis of Recognition

Property and equipment are tangible items that are held for servicing, or for administrative purposes, and are expected to be used during more than one year.

Property and equipment are recognised if it is probable that future economic benefits associated with the asset will flow to the Group and cost of the asset can be reliably measured.

Basis of Measurement

An item of property and equipment that qualifies for recognition as an asset is initially measured at its cost. Cost includes expenditure that is directly attributable to the acquisition of the asset and cost incurred subsequently to add to or replace a part of it. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use and the costs of dismantling and removing the items and restoring at the site on which they are located and capitalised borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalised as a part of computer equipment.

When parts of an item of property and equipment have different useful lives, they are accounted for as separate items (major components) of property & equipment.

The Company and Group apply the cost model to property and equipment and records at cost of purchase or construction together with any incidental expenses thereon less accumulated depreciation and any accumulated impairment losses.

Subsequent Cost

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

Repairs & Maintenance

Repairs and maintenance are charged to the Statement of Profit or Loss during the financial period in which they are incurred.

The cost of major renovations is included in the carrying amount of the assets when it is probable that future economic benefits in excess of the most recently assessed standard of performance of the existing assets will flow to the Company and the Group and the renovation replaces an identifiable part of the asset. Major renovations are depreciated during the remaining useful life of the related asset.

Derecognition

Property and equipment is derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in 'other operating income' in the Statement of Profit or Loss in the year the asset is derecognised.

Depreciation

Depreciation is recognised in Statement of Profit or Loss on a straight line basis over the estimated useful lives of each part of an item of property and equipment since this method most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Depreciation of an asset ceases at the earlier of that the asset is classified as held for sale or the date that the asset is derecognised. Depreciation does not cease when the assets become idle or is retired from active unless the asset is fully depreciated.

The estimated useful lives for the current and comparative years are as follows:

| Class of asset | % per annum | Period |
|---------------------------|----------------|---------------|
| Motor vehicles | 20 -25 | 04 - 05 years |
| Computers and accessories | 20 -25 | 04 - 05 years |
| Building | 5 | 20 years |
| Other assets | 10 -50 | 02 - 10 years |

Borrowing Costs

There were no capitalised borrowing costs relating to the acquisition of property & equipment during the year.

Notes to the Financial Statements

27 Property and Equipment (Contd.)

Information on the Freehold Land and Buildings of the Company

| Location | No. of Buildings | Extent Perches | Buildings sq. ft. | Fair Value Hierarchy | Revalued | Net Book | Net Book | As a % of Total NBV | |
|----------------------------|------------------|----------------|-------------------|----------------------|------------------|-----------|----------|---------------------|--|
| | | | | | Amounts | Value | Value | | |
| | | | | | Land / Buildings | Buildings | Land | | |
| | | | | | Rs.'000 | Rs.'000 | Rs.'000 | | |
| 470, Hendala Road, Wattala | 1 | 64P | 2,200 | Level 3 | 79,400 | 1,190 | 9,961 | 712 | |
| Kurunduwatta, Ekala | | 1A-1R- 2793P | - | - | 95,000 | - | 14,000 | 679 | |
| | | | | | 174,400 | 1,190 | 23,961 | | |

The Market value of the land and building at No. 470, Hendala Road, Wattala was Rs. 75,200,000 and Rs. 4,200,000 respectively as per the valuation carried out in March 2016 by Mr. S.A.M.A. Perera [FIV]. Market value of Kurunduwatta, Ekala land of the Company was Rs. 95,000,000 as per the valuation carried out in August 2017 by Mr. D N Dhammika Baranage RICS [UK], DIV AIS [SL]. The Directors have reviewed the values of the land & buildings as at 31 December 2017 and concluded that there was no impairment.

Title Restriction on Property & Equipment

There were no restrictions existed on the title of the property & equipment of the Group as at the date of the reporting date.

Property & Equipment Pledged as Security for Liabilities

There were no items of property & equipment pledged as securities for liabilities except for lease hold assets.

Compensation from Third Parties for Items of Property & Equipment

There were no compensation received/receivable from third parties for items of property & equipment that were impaired, lost or given up.

Fully Depreciated Property & Equipment

The cost of fully depreciated property & equipment of the Company and the Group which are still in use as at the reporting date are as follows:

| As at 31 December | Company | | Group | |
|---------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Motor vehicles | 36,721 | 34,639 | 36,721 | 34,639 |
| Computer equipments | 147,813 | 131,662 | 189,665 | 157,965 |
| Equipment, furniture & fittings | 87,379 | 70,681 | 113,983 | 86,168 |
| Total | 271,913 | 236,982 | 340,369 | 278,772 |

Temporarily Idle Property & Equipment

There were no property & equipment of the Company and the Group that were temporarily idle as at the reporting date.

Property & Equipment Retired from Active Use

There were no property & equipment of the Company and the Group were retired from active use as at the reporting date.

28 Intangible Assets

Accounting Policy

Basis of Recognition

An intangible asset is recognised only when its cost can be measured reliably, and it is probable that the expected future economic benefits that are attributable to it will flow to the Company/Group in accordance with the Sri Lanka Accounting Standard -LKAS 38 - 'Intangible Assets'.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are stated in the Statement of Financial Position at cost less any accumulated amortisation and any accumulated impairment losses if any.

Subsequent Expenditure

Subsequent expenditure on intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Useful Economic Lives, Amortisation and Impairment

The useful economic lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each reporting date. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and they are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the Statement of Profit or Loss in the expense category consistent with the function of the intangible asset.

| Class of asset | % Per annum | Period |
|-------------------|-------------|-----------|
| Computer Software | 12.5 -25 | 4-8 Years |

Derecognition

Intangible assets are derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss arising on derecognition of the assets is recognised in the Statement of Profit or Loss in the year the assets is derecognised.

Notes to the Financial Statements

28 Intangible Assets (Contd.)

28.a

| For the year ended 31 December | Computer Software Rs.'000 | Total Rs.'000 |
|--|------------------------------|------------------|
| Company | | |
| Cost | | |
| Balance as at 01 January 2016 | 128,008 | 128,008 |
| Additions and improvements during the year | 885 | 885 |
| Balance as at 31 December 2016 | 128,893 | 128,893 |
| Additions and improvements during the year | 226,617 | 226,617 |
| Balance as at 31 December 2017 | 355,510 | 355,510 |
| Accumulated amortisation | | |
| Balance as at 01 January 2016 | 91,697 | 91,697 |
| Amortisation for the year | 10,639 | 10,639 |
| Balance as at 31 December 2016 | 102,336 | 102,336 |
| Amortisation for the year | 26,881 | 26,881 |
| Balance as at 31 December 2017 | 129,217 | 129,217 |
| Net book value | | |
| As at 31 December 2016 - Restated | | 26,557 |
| As at 31 December 2017 | | 226,293 |

28.b

| For the year ended 31 December | Computer Software Rs.'000 | Goodwill Rs.'000 | Total Rs.'000 |
|--|------------------------------|---------------------|------------------|
| Group | | | |
| Cost | | | |
| Balance as at 01 January 2016 | 177,191 | 18,193 | 195,384 |
| Additions and improvements during the year | 2,385 | - | 2,385 |
| Adjustment | (5,251) | - | (5,251) |
| Balance as at 31 December 2016 | 174,325 | 18,193 | 192,518 |
| Additions and improvements during the year | 226,617 | - | 226,617 |
| Transfers during the year | 2,760 | - | 2,760 |
| Balance as at 31 December 2017 | 403,702 | 18,193 | 421,895 |
| Accumulated Amortisation & Impairment | | | |
| Balance as at 01 January 2016 | 112,555 | 18,193 | 130,748 |
| Amortisation for the year | 18,129 | - | 18,129 |
| Adjustment due to amortisation | (4,239) | - | (4,239) |
| Balance as at 31 December 2016 | 126,445 | 18,193 | 144,638 |
| Amortisation for the year | 32,731 | - | 32,731 |
| Balance as at 31 December 2017 | 159,176 | 18,193 | 177,369 |
| Net book value | | | |
| As at 31 December 2016 - Restated | | | 47,880 |
| As at 31 December 2017 | | | 244,526 |

Fully Amortised Intangible Assets

Gross carrying amount of intangible assets which have been fully amortised that are still in use as follows;

| For the year ended 31 December | Company | | Group | |
|--------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Computer Software | 84,052 | 83,749 | 90,076 | 90,041 |

There were no restrictions existed on the title of the intangible assets of the Company and the Group as at the reporting date. Further, there were no items pledged as securities for liabilities.

29 Other Assets

Accounting Policy

The Company and the Group classify all their other assets as mainly comprise of advance payments, commercial paper and sundry receivables.

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 Restated |
| Claims and commission receivables | 14,148 | 18,508 | 14,148 | 18,508 |
| Receivables | 52,062 | 107,237 | 85,877 | 161,502 |
| Advances and pre payments | 121,768 | 46,395 | 153,997 | 63,893 |
| Other accounts | 134,142 | 146,356 | 147,209 | 152,371 |
| Reinsurance assets-insurance contracts | - | - | 283,083 | 289,794 |
| Insurance receivables | - | - | 12,254 | 211,672 |
| Commercial Paper | 445,643 | 414,306 | 445,643 | 414,306 |
| | 767,763 | 732,802 | 1,142,211 | 1,312,046 |
| Less: Allowance for impairment | 449,784 | 414,306 | 449,784 | 420,853 |
| | 317,979 | 318,496 | 692,427 | 891,193 |

30 Due to Banks

Accounting Policy

Due to banks, includes bank overdrafts obtained by the Company and the Group from banks. Subsequent to initial recognition, these are measured at their amortised cost using the EIR method.

| As at 31 December | Company | | Group | |
|-------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Bank overdraft | 123,849 | 201,635 | 129,877 | 224,997 |
| | 123,849 | 201,635 | 129,877 | 224,997 |

Notes to the Financial Statements

31 Due to Customers

Accounting Policy

Due to customers include fixed deposits and saving deposits. Subsequent to initial recognition, these are measured at their amortised cost using the Effective Interest Rate (EIR) method. Amortised cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the EIR. The EIR amortisation is included in 'interest expenses' in the Statement of Profit or Loss. Gains and losses are recognised in the Statement of Profit or Loss when the liabilities are derecognised as well as through the EIR amortisation process.

| As at 31 December | Company | | Group | |
|-------------------|-------------------|-------------------|-------------------|-------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Savings deposits | 868,026 | 728,257 | 868,026 | 728,257 |
| Time deposits | 21,050,843 | 17,790,162 | 21,042,357 | 17,790,162 |
| | 21,918,869 | 18,518,419 | 21,910,383 | 18,518,419 |

32 Debt Issued and Borrowed Funds

Accounting Policy

Debt securities issued represent the funds borrowed by the Company and the Group for long term and short term liquidity fund requirements. Subsequent to initial recognition, these are measured at their amortised cost using the EIR method. Amortised cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the EIR. The EIR amortisation is included in 'interest expenses' in the Statement of Profit or Loss. Gains and losses are recognised in the Statement of Profit or Loss when the liabilities are derecognised as well as through the EIR amortisation process.

| As at 31 December | Company | | Group | |
|---|------------------|------------------|------------------|------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Debentures (Note 32.1) | 5,889,089 | 5,154,869 | 5,889,089 | 5,154,869 |
| Short term borrowings | 1,055,458 | 3,567,918 | 1,055,458 | 3,567,918 |
| Long term borrowings | 1,874,315 | - | 1,874,315 | - |
| Total debt issued and borrowed funds | 8,818,862 | 8,722,787 | 8,818,862 | 8,722,787 |

32.1 Debentures

| ISIN No. | Face value Rs.'000 | Interest rate | Colombo Stock Exchange Listing | Security | Interest Payable Frequency | Allotment Date | Term of Redemption | Company / Group Value as at | |
|---|-----------------------|------------------|---|----------|----------------------------------|-------------------|-----------------------|--------------------------------|------------------|
| | | | | | | | | 2017 Rs.'000 | 2016 Rs.'000 |
| Fixed Rate Debentures | | | | | | | | | |
| LK0186D19194 | 625,110 | 17.50% | listed | Nil | Annually | 28-Mar-13 | 27-Mar-18 | 735,857 | 735,088 |
| LK0186D19210 | 723,190 | 16.70% | listed | Nil | Quarterly | 28-Mar-13 | 27-Mar-18 | 753,659 | 753,581 |
| LK0186D19228 | 166,460 | 16.50% | listed | Nil | Monthly | 28-Mar-13 | 27-Mar-18 | 168,793 | 168,786 |
| LK0186D22669 | 909,770 | 9.00% | listed | Nil | Annually | 13-Nov-14 | 12-Nov-19 | 991,500 | 991,796 |
| LK0186D22677 | 1,090,230 | 8.75% | listed | Nil | Bi Annually | 13-Nov-14 | 12-Nov-19 | 1,132,445 | 1,134,895 |
| LK0186D23824 | 805,760 | 15.00% | listed | Nil | Annually | 03-May-17 | 02-May-22 | 884,335 | - |
| LK0186D23816 | 1,193,230 | 14.50% | listed | Nil | Bi Annually | 03-May-17 | 02-May-22 | 1,221,467 | - |
| LK0186D23808 | 1,010 | 13.89% | listed | Nil | Bi Annually | 03-May-17 | 02-May-22 | 1,033 | - |
| Debenture Redeemed During the Year | | | | | | | | | |
| Fixed Rate | | | | | | | | | |
| LK0186D19202 | 485,240 | 17.25% | listed | Nil | Annually | 28-Mar-13 | 27-Mar-17 | - | 569,943 |
| LK0186D20929 | 674,770 | 14.25% | listed | Nil | Annually | 17-Dec-13 | 16-Dec-17 | - | 771,045 |
| LK0186D20911 | 17,540 | 13.50% | listed | Nil | Quarterly | 17-Dec-13 | 16-Dec-17 | - | 18,136 |
| LK0186D20937 | 11,470 | 13.25% | listed | Nil | Monthly | 17-Dec-13 | 16-Dec-17 | - | 11,599 |
| Total Debentures | 5,514,760 | | | | | | | 5,889,089 | 5,154,869 |

Outstanding number of debentures as at 31 December 2017 consisted of 55,147,600 unsecured redeemable debentures of Rs. 100/- each issued by the Company.

The Company has not repurchased any of its own debt during the year. (2016: Nil)

The Company has not had any default of principal, interest or other breaches with regard to all liabilities during 2017 and 2016.

33 Insurance Provision

Life Insurance Contracts Liabilities (Including Investment Contract Liabilities with DPF)

The liability for life insurance contracts and investment contract with DPF is either based on current assumptions or on assumptions established at inception of the contract, reflecting the best estimate at the time increased with a margin for risk and adverse deviation. All contracts are subject to a liability adequacy test, which reflect management's best current estimate of future cash flows.

The main assumptions used relate to mortality, morbidity, longevity, investment return, expenses, lapse and surrender rates and discount rate. The subsidiary bases mortality, morbidity on standard of the industry.

Mortality tables which reflect historical experience, adjusted when appropriate to reflect the Subsidiary is unique risk exposure, product characteristics, target markets and own claims severity and frequency experience. For these contracts that insure risk related to longevity, prudent allowance is allowable is made for expected future mortality improvements as well as wide ranging

Notes to the Financial Statements

33 Insurance Provision (Contd.)

changes to life style, could insignificant changes to the expected future mortality exposure. Estimates are also made as to future investment income arising from the assets backing life insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments.

Assumptions on future expenses are based on current expenses levels, adjusted for expected expenses inflation is appropriate.

Laps and surrender rates are based on the Subsidiary's historical experience of laps and surrenders.

Discount rates are based on current market risk rates, adjusted for the Subsidiary's own risk exposure.

Non-Life Insurance Contracts Liabilities

Non-Life insurance contract liabilities are recognised when contracts are entered, and premium are charged. These liabilities are known as the outstanding claims provision, which are based on the estimated ultimate cost of all claims incurred but not settled at the reporting date, whether reported or not, together with related claims handling costs and reduction for the expected value of salvage and other recoveries. Delays can be experienced in the notification and settlement of the certain types of claims, therefore the ultimate cost of these cannot be known with certainty at the reporting date. The liability is calculated at the reporting date using a range of standard actuarial claim projection techniques. The liabilities are not discounted for the time value of money. No provision for equalisation or catastrophe reserves is recognised. The liabilities are derecognised when the contract expires, is discharged or is cancelled.

The provision for unearned premiums represents premiums received for risks that have not yet expired. Generally, the reserve is released over the term of the contract and is recognised as premium income. At each reporting date, the Group receives its unexpired risk and a liability adequacy test is performed to determine whether there is any overall excess of expected claims and deferred acquisition costs over unearned premiums. This calculation uses current estimates of future contractual cash flows after taking account of the investment return expected to arise on assets relating to the relevant non-life insurance technical provisions. If these estimates show that the carrying amount of the unearned premiums is inadequate, the deficiency is recognised in the Statement of Profit or a Loss by setting up a provision for liability adequacy.

This note indicates the liability on account of policyholders which has been actuarially valued and claims/benefits due to life policyholders, which remain unclaimed to the reporting date.

33.1 Insurance Provision - Life

| As at 31 December | Group | |
|----------------------------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Balance as at 1 January | 495,171 | 425,231 |
| Increase in life fund | 13,359 | 69,940 |
| | 508,530 | 495,171 |
| Fair value reserve | 1,285 | (16,803) |
| | 509,815 | 478,368 |
| Unclaimed benefits | 37,211 | 35,890 |
| Balance as at 31 December | 547,026 | 514,258 |

Insurance Provision - Life

Long-term insurance contract liabilities included in the life insurance fund result primarily from traditional non-participating life insurance products. Short-duration contract liabilities are primarily accident and health insurance products. The insurance provision has been established based upon the following:

- interest rates which vary by product and as required by regulations issued by the Insurance Board of Sri Lanka.
- mortality rates based on published mortality tables adjusted for actual experience as required by regulations issued by the Insurance Board of Sri Lanka.
- surrender rates based upon actual experience by geographic area and modified to allow for variations in policy form.

33.2 Surplus/Deficit

| As at 31 December | Group | |
|---|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Balance as at 1 January | 495,171 | 425,231 |
| Increase in life fund | 13,359 | 69,940 |
| | 508,530 | 495,171 |
| Fair value reserve | 1,285 | [16,803] |
| Life fund balance as at 31st December | 509,815 | 478,368 |
| Insurance contract liabilities [life] - Gross premium valuation method | [419,524] | [422,005] |
| Surplus/(deficit) as at 31 December | 90,291 | 56,363 |
| Surplus created due to change in valuation method from NPV to GPV [Note 33.3] | - | [35,431] |
| | 90,291 | 20,932 |

The subsidiary - MBSLI allocates assets and expenses to participating and non participating policy funds based on the insurance contract liability for participating and non participating policy funds determined by the consultant actuary Ms. Teja Ranade Gadhoke as at the year end.

Notes to the Financial Statements

33 Insurance Provision (Contd.)

33.3 Surplus Created Due to Change in Valuation Method from NPV to GPV

| As at 31 December | Group | |
|---|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Surplus created due to change in valuation method from NPV to GPV Non-participating policies | - | 3,002 |
| Surplus created due to change in valuation method from NPV to GPV Non-participating policies | - | 32,429 |
| | - | 35,431 |

Valuation of Life Insurance Fund

The valuation of life insurance fund as at 31 December 2017 was made by Ms. Teja Ranade Gadhoke a qualified professional actuary who also determined and certified the surplus created due to change in valuation method from NPV to GPV. As per the report, policy liabilities based on the Gross Premium Valuation method amount to Rs.419 Mn.

Liability Adequacy Test

In the opinion of the consultant actuary Ms Teja Ranade Gadhoke, the liability value is sufficient to meet future benefits and expenses. Hence, no provision was made for premium deficiency.

33.4 Insurance Provision - Non Life

| As at 31 December | Group | |
|---|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 |
| Provision for reported claims by policy holders | 356,018 | 408,237 |
| Provision for claims IBNR | 42,256 | 48,779 |
| Outstanding claims provision | 398,274 | 457,016 |
| Provision for unearned premiums | 31,819 | 324,018 |
| Total non life insurance provision | 430,093 | 781,034 |

A Liability Adequacy Test ("LAT") for non life contract liability was carried out by Mr. Mathew Maguire, FIAA for and on behalf of NMG Financial Services Consulting (Pvt) Limited as at 31 December 2017 as required by SLFRS 4 - Insurance Contracts. The UPR provision of Rs.31.8 Mn set by the Subsidiary - MSBSLI, net of reinsurance, is adequate in relation to the unexpired risks of MBSL Insurance Co Ltd as at 31 December 2017.

As such, there is no premium deficiency to be recognised by the Subsidiary - MSBSLI. In addition according to the consultant actuary's report, IBNR provision of Rs.42.2 Mn is adequate in relation to the claim liability of MBSL Company Ltd as at 31 December 2017.

34 Current Tax Liabilities

Accounting Policy

The Group and the Company are subject to income taxes. Significant judgement is required to determine the total provision for current, deferred and other taxes. Uncertainties exist, with respect to the interpretation of the applicability of laws, at the time of the preparation of these Financial Statements.

Current tax assets are recognised at historical values less impairment. Income tax liabilities are recorded at the amounts expected to be paid.

| As at 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Balance at 01 January | 151,128 | 146,284 | 141,180 | 136,336 |
| Add: Provision for taxation | 35,292 | 62,838 | 43,605 | 74,249 |
| [Over] / under provision of taxes in respect of prior years | [90,258] | - | [90,258] | - |
| Less : Paid during the year | [10,590] | [27,906] | [10,590] | [27,906] |
| Less : Set off during the year | 78,099 | [30,088] | [76,464] | [41,499] |
| Balance as at 31 December | 7,473 | 151,128 | 7,473 | 141,180 |

35 Deferred Tax Liabilities

Accounting Policy

Deferred tax is provided on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised.

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

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

Current tax and deferred tax relating to items recognised directly in equity are also recognised in equity and not in the Statement of Profit or Loss.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

| As at 31 December | Company | | Group | |
|------------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Deferred tax assets [Note 35.2] | [325,148] | [434,082] | [325,148] | [434,082] |
| Deferred tax liability [Note 35.2] | 698,859 | 640,970 | 698,859 | 640,970 |
| | 373,711 | 206,888 | 373,711 | 206,888 |

35.1 Deferred Tax Movement

| | | | | |
|--|----------------|----------------|----------------|----------------|
| Balance as at 01 January | 206,888 | 113,669 | 206,888 | 113,669 |
| Charge for the year | 182,765 | 91,409 | 182,765 | 91,409 |
| Deferred tax charge relating to components of Statements of Comprehensive Income | [15,942] | 1,810 | [15,942] | 1,810 |
| Balance as at 31 December | 373,711 | 206,888 | 373,711 | 206,888 |

Notes to the Financial Statements

35 Deferred Tax Liabilities (Contd.)

35.2 Reconciliation of Deferred Tax Liability

Deferred tax assets and liabilities are attributable to the following:

| As at 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Deferred tax assets | | | | |
| Carry forward tax losses | [251,511] | [374,333] | [251,511] | [374,333] |
| Retirement benefit obligation | [68,634] | [70,688] | [68,634] | [70,688] |
| Actuarial gains/(losses) recognised in Statement of Comprehensive Income | [5,003] | 10,939 | [5,003] | 10,939 |
| | [325,148] | [434,082] | [325,148] | [434,082] |
| Deferred tax liability | | | | |
| Accelerated depreciation allowance for tax purpose [Rentals receivable] | 652,803 | 610,960 | 652,803 | 610,960 |
| Accelerated depreciation allowance for tax purpose [Property and equipment] | 46,056 | 30,010 | 46,056 | 30,010 |
| | 698,859 | 640,970 | 698,859 | 640,970 |
| Net deferred tax liabilities | 373,711 | 206,888 | 373,711 | 206,888 |

Deferred tax has been calculated at the rate of 28%, when computing deferred tax liability, Inland Revenue Act changes were not considered due to non availability of adequate information and instructions.

36 Other Liabilities

Accounting Policy

Other liabilities include accrued expenses and other provisions. These liabilities are recorded at amounts expected to be payable as at the reporting date.

| As at 31 December | Company | | Group | |
|------------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Accrued expenses | 15,898 | 56,220 | 1,016 | 50,104 |
| Payable to employees and suppliers | 193,206 | 134,360 | 225,786 | 178,982 |
| Insurance payable | - | 4,489 | 50,390 | 73,162 |
| Margin accounts | 31,719 | 9,307 | 31,719 | 9,307 |
| Lease creditors | | | | |
| Within 12 months | - | 1,536 | 4,526 | 5,057 |
| Later than 12 months | - | - | 7,851 | 10,686 |
| Other liabilities | 227,142 | 198,262 | 398,425 | 424,736 |
| | 467,965 | 404,174 | 719,713 | 752,034 |

37 Retirement Benefits Obligations

Accounting Policy

The Group measures the present value of the promised retirement benefits for gratuity, which is a defined benefit plan with the advice of an independent professional actuary using the Projected Unit Credit (PUC) method as required by the Sri Lanka Accounting Standards-LKAS 19-‘Employee Benefits’.

Gratuity

In compliance with the Payment Gratuity Act No.12 of 1983 provision is made in the accounts from the first year of service for gratuity payable to employees.

Recognition of Actuarial Gains and Losses

The Group recognises the total actuarial gains and losses that arise in calculating the Group’s obligation in respect of the plan in Other Comprehensive Income during the period in which it occurs.

Funding Arrangements

The gratuity liability is not externally funded.

Accounting Estimates

The actuarial valuation involves making demographic & financial assumptions specified below.

Demographic Assumptions: Mortality rates, Staff turnover, Disability, Retirement age

Financial Assumptions: Rate of discount, Salary Increase, Gratuity Formula, Employee Data, Assets

The mortality rates represent the probabilities of “death” occurring within one year of any given age based on publicly available mortality table issued by Institute of Actuaries, London.

In determining the appropriate long term rate of discount management considers market rates of interest on short term Corporate Bonds/Government Bonds and the anticipated long term rate of inflation.

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Balance as at 01 January | 213,388 | 245,531 | 231,463 | 262,040 |
| Expense recognised in the statement of profit or loss (Note 37.1) | 46,434 | 40,464 | 49,864 | 45,697 |
| Payment made during the year | [14,703] | [33,539] | [18,775] | [35,733] |
| Actuarial gains/[(losses)] recognized in other comprehensive income | 17,867 | [39,068] | 20,448 | [40,541] |
| Balance as at 31 December | 262,986 | 213,388 | 283,000 | 231,463 |
| 37.1 Expense recognised in the statement of profit or loss | | | | |
| Current service cost | 25,841 | 15,911 | 27,708 | 19,338 |
| Interest cost | 20,593 | 24,553 | 22,156 | 26,359 |
| Total | 46,434 | 40,464 | 49,864 | 45,697 |

Notes to the Financial Statements

37 Retirement Benefits Obligations [Contd.]

An actuarial valuation of the retirement benefit obligation was carried out as at 31 December 2017 by Messrs.' Actuarial & Management Consultants (Pvt) Ltd, a firm of professional actuaries. The valuation method used by the actuary to value the liability is the 'Projected Unit Credit' the method recognised by the Sri Lanka Accounting Standard-LKAS 19-'Employee Benefit'.

37.2 Actuarial Assumptions

| | 2017 | 2016 |
|-----------------|-------|-------|
| Discount rate % | 10.40 | 12.11 |

Retirement Age

Expected average working life of the active participants is 7 - 8 years for the year ended 31 December 2017 .

37.3 Sensitivity of Assumptions Employed in Actuarial Valuation

The following table demonstrates the sensitivity to a reasonably possible change in the key assumptions employed with all other variables held constant in the employment benefit liability measurement.

The sensitivity of the Statement of Profit or Loss and Statement of Financial Position is the effect of the assumed changes in discount rate and salary increment rate on the profit or loss and employment benefit obligation for the year.

| Increase/ (Decrease) in Discount Rate | Sensitivity Effect on Statement of Profit or Loss Increase /[(Reduction) in Results for the year (Rs'000) | Sensitivity Effect on Employment Benefit Obligation Increase /[(Decrease) in the Liability (Rs'000) |
|---------------------------------------|---|---|
| 1% | (12.886) | (12.886) |
| [1%] | 14.364 | 14.364 |

* Discount rate is fixed at; 2017 - 10.40%

38 Stated Capital

| As at 31 December | Company | | Group | |
|----------------------------------|--------------------|--------------------|--------------------|--------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Value of shares issue | | | | |
| Balance as at 01 January | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 |
| Balance as at 31 December | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 |
| No. of shares in issue | | | | |
| Balance as at 01 January | 165,874,541 | 165,874,541 | 165,874,541 | 165,874,541 |
| Balance as at 31 December | 165,874,541 | 165,874,541 | 165,874,541 | 165,874,541 |

39 Reserves

39.1 Statutory Reserves

| As at 31 December | Company | | Group | |
|----------------------------------|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Balance as at 01 January | 157,669 | 140,544 | 157,669 | 140,544 |
| Add: Transfers during the year | 20,170 | 17,125 | 20,170 | 17,125 |
| Balance as at 31 December | 177,839 | 157,669 | 177,839 | 157,669 |

Statutory reserve represents the reserve fund of the Company created in terms of the Finance Companies (Capital Funds) Direction No. 01 of 2003 issued by the Central Bank of Sri Lanka.

39.2 Retained Earnings

| As at 31 December | Company | | Group | |
|----------------------------------|-----------------|-----------------------------|-----------------|-----------------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2017 Rs.'000 | 2016 Rs.'000 Restated |
| Balance as at 01 January | 846,191 | 747,408 | 859,584 | 726,298 |
| Add: Profit for the year | 100,851 | 78,650 | 111,858 | 110,879 |
| Transfers to statutory reserves | (20,170) | (17,125) | (20,170) | (17,125) |
| Other comprehensive income | (1,925) | 37,258 | (2,857) | 39,532 |
| Balance as at 31 December | 924,947 | 846,191 | 948,415 | 859,584 |

39.3 Available-for-Sale Reserve

| | | | | |
|---|--------------|-----------------|--------------|-----------------|
| Balance as at 01 January | (21,802) | (4,350) | (36,195) | (8,920) |
| Add: Gains/ (Losses) on remeasuring available-for-sale financial assets | 28,379 | (17,452) | 37,495 | (27,275) |
| Balance as at 31 December | 6,577 | (21,802) | 1,300 | (36,195) |

40 Additional Cash Flow Information

40.1 Analysis of Cash and Cash Equivalents

| | | | | |
|--|----------------|----------------|----------------|----------------|
| Cash and short term funds | 418,885 | 401,301 | 466,139 | 441,357 |
| Due to banks with original maturity less than three months | (123,849) | (201,635) | (129,877) | (224,997) |
| | 295,036 | 199,666 | 336,262 | 216,360 |

40.2 Change in Operating Assets

| | | | | |
|---------------------------------------|--------------------|--------------------|--------------------|--------------------|
| Loans and advances given to customers | (1,701,662) | (3,826,220) | (1,624,839) | (3,799,444) |
| Other operating assets | (96,041) | (48,641) | 105,011 | (162,688) |
| Adjustment for impairment | (244,231) | (24,239) | (245,206) | (27,959) |
| | (2,041,934) | (3,899,100) | (1,765,033) | (3,990,091) |

40.3 Change in Operating Liabilities

| | | | | |
|-----------------------------|------------------|------------------|------------------|------------------|
| Due to customers | 3,400,450 | 2,672,113 | 3,391,964 | 2,672,113 |
| Other operating liabilities | 63,791 | 47,334 | (32,321) | (204,576) |
| Insurance provision | - | - | (318,173) | 338,702 |
| | 3,464,241 | 2,719,447 | 3,041,470 | 2,806,239 |

Notes to the Financial Statements

40 Additional Cash Flow Information (Contd.)

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------------------|-----------------|-----------------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2017 Rs.'000 | 2016 Rs.'000 Restated |
| 40.4 Other Non-Cash Items Included in Profit Before Tax | | | | |
| Loss on disposal of quoted shares | 24,296 | 2,781 | 23,209 | 7,515 |
| Interest accrued on government securities | (41,921) | [146,151] | (41,921) | [146,151] |
| Gain on sale of property and equipment | (3,654) | [32,909] | (4,718) | [35,990] |
| Net (gain)/loss on financial assets designated at FVPL | (5,624) | 61,096 | (4,771) | 58,226 |
| Impairment charges | 300,420 | 257,130 | 245,206 | 27,959 |
| Depreciation and amortisation | 109,025 | 75,047 | 128,186 | 101,616 |
| | 382,542 | 216,994 | 345,192 | 13,175 |

Other financial disclosures

This section provides information on related party disclosures and other disclosures required by the Sri Lanka Accounting Standards.

41 Related Party Disclosure

The Company / Group carried out transactions in the ordinary course of its business with parties who are defined as related parties in Sri Lanka Accounting Standard-LKAS 24-'Related Party Disclosures'.

41. a Transactions with Key Management Personal (KMP)

According to Sri Lanka Accounting Standard-LKAS 24, Key Management Personnel are those having authority and responsibility for planning, directing and controlling the activities of the entity. Accordingly, the directors of the Company/Group (including executive and non-executive directors), chief executive officer, chief operating officer and corporate management committee have been classified as KMP of the Company.

41. b Directors Interest in Contracts/ Transactions with Related Parties

Dr. S. Lokuhewa, Mr. D. M. Gunasekara, Mr. W. P. R. P. H. Fonseka, Mr. K. B. S. Bandara, Mr. N. Perera, Mr. S. N. Dayaratne, Mr. S. P. Arsakularatne, Mr. R. M. D. V. Jayabahu [Alternate Director], Mr. D. M. L. B. Dassanayake [Alternate Director] were directors of the Company as at 31 December 2017.

41. c Transactions with Key Management Personnel

Remuneration to Key Management

| For the year ended 31 December | Company | | Group | |
|---|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| (a) Remuneration to Board of Directors | | | | |
| Short term employee benefits | 6,301 | 4,123 | 6,301 | 7,367 |
| | 6,301 | 4,123 | 6,301 | 7,367 |
| (b) Remuneration to Corporate Management | | | | |
| Short term employee benefits | 78,091 | 69,146 | 78,091 | 90,814 |
| Post employment benefits | - | 18,977 | - | 18,977 |
| | 78,091 | 88,123 | 78,091 | 109,791 |

Transactions, arrangements and agreements with key management personnel

| | Company | | | |
|---|--------------------|-----------------|----------------------|-----------------|
| | Board of Directors | | Corporate Management | |
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| [a] Items in Statement of Financial Position | | | | |
| Assets - Loans and receivables | - | - | 23,062 | 17,296 |
| Liabilities - Due to customers | 27 | - | 20,073 | 4,861 |
| [b] Items in Statement of Profit or Loss | | | | |
| Interest income | - | - | 690 | 897 |
| Interest expence | 1 | - | 1,295 | 523 |

In addition to the above, the Company has also provided company maintained vehicles to the chairman and the chief executive officer in line with the approved employment terms of the Company.

Share Transactions With Key Management Personnel

For the year ended 31 December

| | Company | |
|-----------------------------|---------|------|
| | 2017 | 2016 |
| No. of ordinary shares held | 21 | 21 |

41. d Terms and Conditions of Transactions with Related Parties

The transactions mentioned in Note 41.e arose from the ordinary course of business. The interest charged to and by related parties are at normal commercial rates. Outstanding balances at the year end are unsecured except Rs. 250 Mn OD facility obtained from Bank Of Ceylon. Such OD facility is secured by leasing facilities. There have been no guarantees provided or received for any related party receivables or payables. For the year ended 31 December 2017, the Company/Group has not made any provision for impairment relating to amounts owed by related parties.

41.e Details of significant related party transactions that have been carried out in the ordinary course of business in an arms length basis with entities are disclosed below.

Company

| Nature of Transactions | Income/[Expenses] Recognised During the Year | | Assets/[Liabilities] as at 31 December | |
|---|--|-----------------|--|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| | | | | |
| Transactions with parent company | | | | |
| Bank of Ceylon | | | | |
| Money market loan | (81,951) | [110,401] | (310,000) | [1,320,000] |
| Debenture | [210,691] | [155,177] | [2,322,440] | [1,626,020] |
| Bank fee and charges | [1,734] | [2,819] | - | - |
| Interest received-REPO | 30,841 | 2,162 | 200,000 | 263,466 |
| Interest paid-REPO | - | [62] | - | - |
| Fixed deposit and savings | 344 | - | 262,000 | - |
| Transactions with subsidiary | | | | |
| MBSL Insurance Company Limited | | | | |
| Insurance agency commission | 6,066 | 16,883 | - | - |
| Insuranse expenses | [16,836] | [10,235] | - | - |
| Travel insurance | [6] | - | - | - |
| Fixed deposits and savings | [989] | - | [8,486] | - |
| Loans and advances | 2,451 | - | 77,451 | - |

Notes to the Financial Statements

41 Related Party Disclosure (Contd.)

| Nature of Transactions | Income/[(Expenses)] Recognised During the Year | | Assets/[(Liabilities)] as at 31 December | | |
|---|--|-----------------|--|-----------------|-----------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 | |
| Transactions with other companies | | | | | |
| BOC Property Development and Management Company Limited | Rent paid | (70,690) | (55,383) | - | - |
| | Electricity, water, office maintenance, rates | (15,457) | (15,459) | - | - |
| | Fixed Deposits and savings | (4,013) | - | (70,000) | - |
| Grand Oriental Hotel | Staff training | (188) | (659) | - | - |
| | Meeting expenses | - | (229) | - | - |
| Credit Information Bureau of Sri Lanka | Dividend received | 720 | 234 | - | - |
| | CRIB charges | (11,929) | (15,182) | - | - |
| Ceybank Asset Management Limited | Fixed Deposits and Savings | (4,723) | (79) | - | (14,036) |
| Lanka Clear (Pvt) Ltd | Slips processing charges | (271) | (240) | - | - |
| | Charges for online data transfer process | - | (14) | - | - |
| | Fixed deposits and savings | (27,184) | (2,864) | - | (184,710) |
| | Annual membership fee | (327) | - | - | - |
| Group | | | | | |
| Subsidiary-MBSL Insurance Company Limited | Gross written premium | 6,854 | 26,490 | - | - |
| | Premium receivable | - | - | (155) | 785 |
| | Claims incurred | 3,724 | 26,445 | - | - |

42 Fair Value of Financial Instruments

Determination of Fair Value and Fair Value Hierarchy

Accounting Policy

Financial Instruments Recorded at Fair Value

The following is a description of how fair values are determined for financial instruments that are recorded at fair value using valuation techniques. These incorporate the Company's/Group's estimate assumptions that a market participant would make when valuing instruments.

Financial Assets at Fair Value Through Profit or Loss- Held-for-Trading

Held-for-trading financial assets valued using valuation techniques primarily consist of quoted investments. These quoted assets are valued using quoted market price in an active market of each securities.

Financial Assets and Liabilities Carried at Amortised Cost

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated based on the discounted cash flow approach. This approach employs the current market interest rates of similar financial instruments as a significant unobservable input in measuring the fair value and hence it is categorised under level 3 in the fair value hierarchy.

Valuation Model

For all financial instruments where fair values are determined by referring to externally quoted prices or observable pricing inputs to models, independent price determination or validation is obtained. In an active market, direct observation of a traded price may not be possible. In these circumstances, the Company/Group uses alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable.

A. Determination of Fair Value and Fair Value Hierarchy

The Company and Group use the following hierarchy for determining and disclosing the fair value of financial instruments by valuation techniques:

Level 1: Quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: Other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly;

Level 3: Techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

| As at 31 December | Company | | | | | | | |
|---|--------------------|--------------------|--------------------|------------------|--------------------|--------------------|--------------------|------------------|
| | 2017 | | | | 2016 | | | |
| | Rs.'000 Level 1 | Rs.'000 Level 2 | Rs.'000 Level 3 | Rs.'000 Total | Rs.'000 Level 1 | Rs.'000 Level 2 | Rs.'000 Level 3 | Rs.'000 Total |
| Financial assets | | | | | | | | |
| Financial investments | | | | | | | | |
| - held-for-trading | 231,264 | - | - | 231,264 | 323,655 | - | - | 323,655 |
| | 231,264 | - | - | 231,264 | 323,655 | - | - | 323,655 |
| Financial investments - available-for-sale | | | | | | | | |
| Government securities | 640,791 | - | - | 640,791 | 2,694,335 | - | - | 2,694,335 |
| Unquoted investments | - | - | 51,554 | 51,554 | - | - | 41,310 | 41,310 |
| Unit trust | - | 1,122,836 | - | 1,122,836 | - | - | - | - |
| | 640,791 | 1,122,836 | 51,554 | 1,815,181 | 2,694,335 | - | 41,310 | 2,735,645 |
| | 872,055 | 1,122,836 | 51,554 | 2,046,445 | 3,017,990 | - | 41,310 | 3,059,300 |
| | | | | | | | | |
| As at 31 December | Group | | | | | | | |
| | 2017 | | | | 2016 | | | |
| | Rs.'000 Level 1 | Rs.'000 Level 2 | Rs.'000 Level 3 | Rs.'000 Total | Rs.'000 Level 1 | Rs.'000 Level 2 | Rs.'000 Level 3 | Rs.'000 Total |
| Financial assets | | | | | | | | |
| Financial investments | | | | | | | | |
| - held-for-trading | 238,252 | - | - | 238,252 | 331,586 | - | - | 331,586 |
| | 238,252 | - | - | 238,252 | 331,586 | - | - | 331,586 |
| Financial investments - available-for-sale | | | | | | | | |
| Government securities | 978,638 | - | - | 978,638 | 3,049,945 | - | - | 3,049,945 |
| Unquoted investments | - | - | 51,554 | 51,554 | - | - | 42,287 | 42,287 |
| Unit trust | - | 1,161,650 | - | 1,161,650 | - | 34,583 | - | 34,583 |
| | 978,638 | 1,161,650 | 51,554 | 2,191,842 | 3,049,945 | 34,583 | 42,287 | 3,126,815 |
| | 1,216,890 | 1,161,650 | 51,554 | 2,430,094 | 3,381,531 | 34,583 | 42,287 | 3,458,401 |

Notes to the Financial Statements

42 Fair Value of Financial Instruments (Contd.)

Accounting Policy

Financial Instruments Recorded at Fair Value

The following is a description of how fair values are determined for financial instruments that are recorded at fair value using valuation techniques incorporating Group's estimate of assumptions that a market participant would make when valuing the instruments.

Financial Instruments Carried at Fair Value

The fair value is the amount for which a financial asset could be exchanged between knowledgeable, willing parties. If an active market exists, the market price is applied. If an active market does not exist, which is the case for a number of financial assets and liabilities, a discounted cash flow or generally accepted estimation and valuation techniques based on market conditions at the reporting date are used to calculate an estimated value.

Financial Investments Available-for-Sale

Available-for-sale financial assets valued using valuation techniques or pricing models primarily consist of government debt securities and unquoted equity securities.

These assets are valued using models that use both observable and unobservable data. The un-observable inputs to the models include assumptions regarding the future financial performance of the investee, its risk profile, and economic assumptions regarding the industry and geographical jurisdiction in which the investee operates.

Other Financial Assets Designated at Fair Value Through Profit or Loss

Other financial assets designated at fair value through profit or loss valued using the market price since an active market exists.

Day 1 Profit

When the transaction price differs from the fair value of other observable current market transactions in the same instrument, the Group amortise the difference between the transaction price and fair value (i.e. Day 1 profit or loss) over time on an applicable basis in interest income. The table below shows the movement in the aggregate profit not recognised when financial instruments were initially recognised ('Day 1 Profit').

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Balance as at 1 January | 40,297 | 51,396 | 40,297 | 51,396 |
| Reduction due to passage of time | [20,585] | (16,840) | [20,585] | (16,840) |
| Deferral of profit on new transactions | 75,898 | 16,008 | 75,898 | 16,008 |
| Derecognition of the instruments | [19,381] | (10,267) | [19,381] | (10,267) |
| Balance as at 31 December | 76,229 | 40,297 | 76,229 | 40,297 |

Set out below is a comparison, by class, of the carrying amounts and fair values of the Group's financial instruments that are not carried at fair value in the Financial Statements. This table does not include the fair values of non-financial assets and non-financial liabilities.

| As at 31 December | Company | | | | Group | | | |
|--|-------------------------------|--------------------------|-------------------------------|--------------------------|-------------------------------|--------------------------|-------------------------------|--------------------------|
| | 2017 | | 2016 | | 2017 | | 2016 | |
| | Rs.'000 Carrying Amount | Rs.'000 Fair Value | Rs.'000 Carrying Amount | Rs.'000 Fair Value | Rs.'000 Carrying Amount | Rs.'000 Fair Value | Rs.'000 Carrying Amount | Rs.'000 Fair Value |
| Financial assets | | | | | | | | |
| Placements with banks & financial institutions | 1,509,597 | 1,509,597 | 118,933 | 118,933 | 1,597,785 | 1,597,785 | 262,319 | 262,319 |
| Bills receivable | 494,096 | 494,096 | 739,403 | 739,403 | 494,096 | 494,096 | 739,403 | 739,403 |
| Loans and advances to customers | 12,598,133 | 12,598,133 | 11,320,845 | 11,320,845 | 12,592,956 | 12,592,956 | 11,392,491 | 11,392,491 |
| Lease and hire purchase receivable | 15,661,432 | 15,661,432 | 14,991,751 | 14,991,751 | 15,661,432 | 15,661,432 | 14,991,751 | 14,991,751 |
| Financial investments - held-to-maturity | 479,362 | 484,934 | 57,766 | 57,508 | 479,362 | 484,934 | 57,766 | 57,508 |
| Other assets | 46,865 | 46,865 | 34,454 | 34,454 | 46,865 | 46,865 | 34,454 | 34,454 |
| Total | 30,789,485 | 30,795,057 | 27,263,152 | 27,262,894 | 30,872,496 | 30,878,068 | 27,478,184 | 27,477,926 |
| Financial liabilities | | | | | | | | |
| Due to customers | 21,918,869 | 21,918,869 | 18,518,419 | 18,518,419 | 21,910,383 | 21,910,383 | 18,518,419 | 18,518,419 |
| Debt issued and borrowed funds | 8,818,862 | 8,818,862 | 8,722,787 | 8,722,787 | 8,818,862 | 8,818,862 | 8,722,787 | 8,722,787 |
| Other liabilities | 338,072 | 338,072 | 110,717 | 110,717 | 338,072 | 338,072 | 110,717 | 110,717 |
| Total | 31,075,803 | 31,075,803 | 27,351,923 | 27,351,923 | 31,067,317 | 31,067,317 | 27,351,923 | 27,351,923 |

Fair Value of Financial Assets and Liabilities not Carried at Fair Value

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the Financial Statements:

Assets for which Fair Value Approximates Carrying Value

For financial assets and financial liabilities that have a short-term maturity it is assumed that the carrying amounts approximate to their fair value.

Fixed Rate Financial Instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates for similar financial instruments.

43 Events after the Reporting Period

43.1 Company

No circumstances have arisen since the reporting date which would require adjustments to, or disclosure in the Financial Statements.

43.2 Group

MBSL Insurance Company Limited

On 14 February, 2018 MBSL [the company] as a major shareholder of the Subsidiary MBSLI has published an invitation for expression of interest to invest in a significant minority stake in MBSL Insurance Company Limited for which for parties have already expressed their interest and the process of selecting is still going on.

Notes to the Financial Statements

44 Going Concern of Subsidiary

a. Going Concern of MBSL Insurance Company Limited

The MBSL Insurance Company Limited has incurred a loss of Rs. 53,579,000/- for the year ended 31 December 2017 (2016 loss of Rs. 231,179,000/-) and accumulated losses of Rs. 1,048,612,000/- as at 31 December 2017 (2016 - Rs. 972,726,000/-). It should also be noted that the net assets are less than half of the stated capital and face a serious loss of capital situation in term of Section 220 of the Companies Act No.07 of 2007.

The non-life business does not fulfill the minimum required thresholds set for Capital Adequacy Ratio and Total available Capital by the Regulation of Insurance Industry Act, No.43 of 2000, "the Solvency Margin (Risk Based Capital) Rules 2015" while the life business does not fulfill the minimum required threshold set for total available capital.

The subsidiary has also not segregated the long-term insurance business and the general insurance business being carried on by it into two separate companies in accordance with Section 53 of Regulation of Insurance Industry (Amendment) Act No. 03 of 2011.

However, the financial statements of the subsidiary are prepared with the assumption that the subsidiary is able to continue as going concern with the written undertaking given by the parent company Merchant Bank of Sri Lanka & Finance PLC, as the controlling shareholders of MBSL Insurance Company Limited which holds 84.12% of the issued capital of MBSL Insurance Company, to infuse capital in to MBSL Insurance Company Limited as and when required.

45 Restatement of Comparatives

The restatement had and impact on the following components of financial statements for the year ended 31st December 2016.

45.1 Income Statement

| | Note | Company | | | Group | | |
|---|------|--------------|-------------|----------|--------------|-------------|----------|
| | | Current | As Reported | Impact | Current | As Reported | Impact |
| | | Presentation | Previously | | Presentation | Previously | |
| | | 2016 | 2016 | 2016 | 2016 | 2016 | |
| | | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| Fee and commission income | 1 | 131,483 | 41,455 | 90,028 | 190,723 | 100,695 | 90,028 |
| Fee and commission expenses | 2 | (37,813) | - | (37,813) | (103,487) | (65,674) | (37,813) |
| Other operating income | 1 | 69,922 | 159,950 | (90,028) | 113,561 | 203,589 | (90,028) |
| Depreciation of property, equipment & investment properties | 4 | (64,408) | (63,572) | (836) | (83,487) | (82,651) | (836) |
| Amortisation of intangible assets | 3 | (10,639) | (14,098) | 3,459 | (18,129) | (21,588) | 3,459 |
| Other operating expenses | 2 | (641,940) | (670,156) | 28,216 | (915,175) | (943,391) | 28,216 |

45.2 Statement of Financial Position

Assets

| | | | | | | | |
|------------------------|-----|---------|---------|----------|---------|---------|----------|
| Property and equipment | 4 | 316,511 | 312,337 | 4,174 | 358,266 | 354,092 | 4,174 |
| Intangible assets | 3 | 26,557 | 37,705 | (11,148) | 47,880 | 59,028 | (11,148) |
| Other assets | 5 | - | - | - | 891,193 | 910,918 | (19,725) |
| Retained earnings | 1-5 | 846,191 | 853,165 | (6,974) | 859,584 | 886,283 | (26,699) |

45.3 Statement of Cash Flows

| | | | | | | | |
|--------------------------------------|-----|-----------|-----------|---------|-----------|-----------|----------|
| Cash flows from operating activities | 1,2 | (793,684) | (784,087) | (9,597) | (998,260) | (986,158) | (12,102) |
| Cash flows from investing activities | 3,4 | (474,508) | (484,105) | 9,597 | (648,100) | (660,202) | 12,102 |

Comparative figures have been changed due to following classification changes for the year 2016.

1. Insurance commission which was categorized under other operating income reclassified as fee and commission income.
2. Fee related expenses which was classified as other operating expenses reclassified as fee and commission expenses.
3. Computer software which was recognised under operating expense recognised as intangible assets.
4. Purchase of computer accessories which was recognised as operating expenses recognised as property and equipment.
5. Additional income tax liability to the year of assessment 2013/14 in respect of the interest income of MBSLI General insurance business has been charged to the profit or loss and setoff against the tax credit .

46 Financial Reporting by Segment

Accounting Policy

The Group's segmental reporting is based on the business segment.

A segment is a distinguishable component of the Group that is engaged in providing products and services. (Business segments, which is subject to risks and rewards that are different from those of other segments).

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

The accounting policies adopted for segment reporting are those accounting policies adopted for preparing the Financial Statements of the Group.

Inter -segment transfers are accounted for at competitive fair market prices charged to intercompany counterparts for similar services. Such services are eliminated on consolidation.

As per the provision of Sri Lanka Financial Reporting Standards (SLFRS 8), the operating segment of the Group has been identify based on the products and services offered by the Group of which level of risks and rewards are significantly differ from one another.

Top management of the Group consider the operating results and condition of its business segment in their decision making process and performance evaluation. Types of products and services from which each operating segment derives its revenues describes as follows:

Lease & Hire-Purchase

This segment includes Leasing and Hire Purchase products offered to the customers.

Corporate and Retail Credit

This segment includes Loan products offered to the customers.

Corporate Advisory and Capital Markets

This segment includes Capital market and corporate advisory services.

Insurance

Insurance business segment includes life and general insurance.

Notes to the Financial Statements

46 Financial Reporting By Segment (Contd.)

| Group | Leasing | | Corporate & Retail | |
|---|-------------------|-------------------|--------------------|-------------------|
| | | | Credit | |
| For the year ended 31 December | 2017 | 2016 | 2017 | 2016 |
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| Revenue from external customers | | | | |
| Interest and similar income | 3,044,385 | 2,511,325 | 2,648,437 | 1,876,346 |
| Interest and similar expenses | 1,611,244 | 1,281,274 | 1,329,109 | 921,443 |
| Net interest income | 1,433,141 | 1,230,051 | 1,319,328 | 954,903 |
| Other income | 66,052 | 43,283 | 144,348 | 9,702 |
| Total operating income | 1,499,193 | 1,273,334 | 1,463,676 | 964,605 |
| Impairment charges for loans and other losses | [114,431] | [23,836] | [185,989] | [403] |
| Net operating income | 1,384,762 | 1,249,498 | 1,277,687 | 964,202 |
| Depreciation of property, equipment & investment properties | 35,686 | 30,456 | 29,438 | 21,903 |
| Amortisation of intangible assets | 11,678 | 5,031 | 9,633 | 3,618 |
| Segment result | 522,168 | 503,890 | 566,137 | 427,989 |
| Profit / (loss) from operations after impairment from subsidiary investments | | | | |
| Value Added Tax on financial services | | | | |
| Share of associate company's profit/(loss) before tax | | | | |
| Profit/(loss) before income tax | | | | |
| Income tax expense | | | | |
| Profit/(loss) for the year | | | | |
| Assets | | | | |
| Capital expenditures | | | | |
| Property and equipment | 35,757 | 65,938 | 30,154 | 53,467 |
| Intangible assets | 95,873 | 395 | 80,849 | 321 |
| Total assets | 15,661,432 | 14,991,751 | 13,129,655 | 12,156,037 |
| Total liabilities | 13,750,012 | 12,843,264 | 11,527,229 | 10,413,940 |

| Corporate Advisory & Capital Markets | | Insurance | | Eliminations / Unallocated | | Total | |
|---|-----------|-----------|-----------|-------------------------------|-----------|------------|------------|
| 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| | | | | | | | |
| 20,514 | 18,469 | 99,326 | 115,233 | 443,950 | 331,634 | 6,256,612 | 4,853,007 |
| 32,124 | 49,232 | 17,560 | 66,627 | 718,588 | 391,981 | 3,708,625 | 2,710,557 |
| (11,610) | (30,763) | 81,766 | 48,606 | (274,638) | (60,347) | 2,547,987 | 2,142,450 |
| | | | | | | | |
| (10,549) | (21,835) | 228,814 | 248,310 | (32,873) | 18,614 | 395,792 | 298,074 |
| (22,159) | (52,598) | 310,580 | 296,916 | (307,511) | (41,733) | 2,943,779 | 2,440,524 |
| | | | | | | | |
| - | - | (975) | (3,720) | (56,189) | - | (245,206) | (27,959) |
| (22,159) | (52,598) | 309,605 | 293,196 | (251,322) | (41,733) | 2,698,573 | 2,412,565 |
| | | | | | | | |
| 711 | 1,170 | 13,311 | 19,079 | 16,309 | 10,879 | 95,455 | 83,487 |
| 233 | 193 | 5,850 | 7,490 | 5,337 | 1,797 | 32,731 | 18,129 |
| (33,733) | (142,344) | (46,436) | (220,524) | (590,331) | (212,018) | 417,805 | 356,993 |
| | | | | | | 417,805 | 356,993 |
| | | | | | | (179,403) | (111,730) |
| | | | | | | 1,059 | (5,437) |
| | | | | | | 239,461 | 239,826 |
| | | | | | | (136,111) | (165,658) |
| | | | | | | 103,349 | 74,168 |
| | | | | | | | |
| 544 | 1,640 | 151 | 5,858 | 18,065 | 33,192 | 84,671 | 160,095 |
| 1,458 | 10 | - | 1,500 | 48,437 | 159 | 226,617 | 2,385 |
| | | | | | | | |
| 238,252 | 372,896 | 21,117 | 77,306 | 7,866,510 | 6,016,748 | 36,916,966 | 33,614,738 |
| | | | | | | | |
| 209,174 | 319,455 | 1,332,359 | 1,684,583 | 6,839,036 | 5,233,638 | 33,657,810 | 30,494,880 |

Notes to the Financial Statements

47 Contingent Liabilities and Commitments

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is not probable or cannot be readily measured as defined in the Sri Lanka Accounting Standard - LKAS 37 - 'Provisions, Contingent Liabilities and Contingent Assets'. Contingent liabilities are not recognised in the Statement of Financial Position but are disclosed unless its occurrence is remote.

The table below shows the Group's maximum credit risk exposure for commitments and guarantees.

| As at 31 December | Company | | Group | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2017 Rs.'000 | 2016 Rs.'000 | 2017 Rs.'000 | 2016 Rs.'000 |
| Financial guarantees & claims to the customers | 167,712 | 132,265 | 183,166 | 616,478 |
| Total commitments and contingencies | 167,712 | 132,265 | 183,166 | 616,478 |

In the normal course of business, the Company makes various irrevocable commitments and incurs certain contingent liabilities with legal recourse to its customers. Even though these obligations may not be recognised on the Statement of Financial Position, they do contain credit risk and therefore form part of the overall risk of the Company. No material losses are anticipated as a result of these transactions.

Further, the Company has issued a letter of comfort to the Subsidiary, MBSL Insurance Company Limited to provide financial support in any difficulty.

Company

47.1 Pending Litigations

In the normal course of business, the Company incurs certain contingent liabilities with legal recourse to its customers and would be party to litigation due to its operations.

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|---|---|---|
| 1 | 43156/MR DC - Colombo | This action has been filed against MBSL for releasing the leased article to the third party who was authorized in writing by the lessee to receive the certificate of registration etc. from MBSL. Following the full settlement of the lease facility by the third party, MBSL released the vehicle and the lessee thereafter filed this action against MBSL claiming damages thus disputing the signature on his own letter of authority. | Plaintiff's action dismissed on 15/07/2016. Appeal pending. |
| 2 | 421/05 DC - Kandy (HCCP/CA/LA 38/2015) | This action has been filed challenging the repossession of the leased article. However, the repossession has been effected in strict conformity with the provisions of the lease agreement. Therefore, no liability could be passed down to MBSL and this action will not be successful. Trial still proceeding - Provisional Court of Appeal made preliminary order favouring on MBSL. The DC action was dismissed by court in December 2017. | DC action dismissed. |
| 3 | 4124/M DC - Gampaha | The Lessee/ Plaintiff filed this action claiming damages for wrongful re-possession of the vehicle. However the injunction sought by the lessee/ plaintiff preventing MBSL from disposing the vehicle in issue was disallowed. | Order on 07/06/2018. |
| 4 | 23840/M DC - Anuradhapura | The Lessee/ Plaintiff filed this action claiming damages for wrongful re-possession of the vehicle and a declaration that the MBSL has violated the provisions of the Lease Agreement and matter is presently proceeding in Trial. | Order on 10/05/2018. |
| 5 | DMR/3675/11 DC - Colombo | This action has been filed against the MBSL to recover Rs.2,500,000/- as damages for refusal to grant a hire purchase facility. | Further trial on 09/05/2018. |
| 6 | 13436/M DC - Kurunegala | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing the death of the Plaintiff's wife in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the hire purchase agreement the liability falls entirely on the registered owner and the Insurer. | Settlement to be recorded on 20/06/2018. |
| 7 | 13434/M DC - Kurunegala | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing the death of the Plaintiff's wife in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the hire purchase agreement the liability falls entirely on the registered owner and the Insurer. | Settlement to be recorded on 20/06/2018. |
| 8 | 13435/M DC - Kurunegala | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing serious injuries to the Plaintiffs in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the hire purchase agreement the liability falls entirely on the registered owner and the Insurer. | Settlement to be recorded on 20/06/2018. |

Notes to the Financial Statements

47 Contingent Liabilities and Commitments [Contd.]

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|---|--|--|
| 9 | 13437/M DC - Kurunegala | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing the death of the Plaintiff's father in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the hire purchase agreement the liability falls entirely on the registered owner and the Insurer. | Settlement to be recorded on 20/06/2018. |
| 10 | Claim- 01/2014 HC Hambantota | This is a claim action arising from the execution of writ by MBSL in case no.HC/ARB/2237/2010. The Petitioner is seeking the release of seized articles. | Petition dismissed on 08/03/2018. |
| 11 | Appeal No.134/2009 [F] Civil Appellate Court Gampaha | This is an appeal instituted against the order of DC Gamapaha in favour of MBSL in case no.426/L filed by a Mortgagor seeking to nullify the Mortgage bond executed by her to secure a financial leasing facility obtained in 1998. Against the dismissal of that action she filed this appeal and the hearing has been concluded. | Judgement reserved for delivery in due course. |
| 12 | DMR/000578/13 DC-Kandy | The Plaintiff has filed this action against the registered owner of the vehicle and MBSL seeking damages for injuries caused to the Plaintiff in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the hire purchase agreement the liability falls entirely on the registered owner and the Insurer. | Case was laid by due to non-availability of instructions from the plaintiff. |
| 13 | LT application No.13/305/02 | This is an application filed by an ex. Employee of MBSL in the Labour Tribunal seeking re-instatement and the payment of back wages. This employee's service was terminated due to a financial fraud committed by him when functioning as the Cashier. On a complaint made by MBSL the Colombo Fraud Bureau through the Attorney General's Department filed criminal action bearing No.HC/1676/2004 in the Criminal High Court of Colombo. Trial is being heard at present and the MBSL witnesses have finished their evidence. In the event that this criminal action is decided against this employee the question of reinstatement and payment of back wages is most unlikely to arise. | The hearing of the LT application kept in abeyance pending the final determination of the High Court Action. |
| 14 | CL/146/2015 [HC/ Civil/MR/529/08] DC - Kantale | This action was instituted by a claimant claiming the articles seized by MBSL through Fiscal in the execution of writ in case no. HC/Civil/529/MR/2008. | Further inquiry on 22/05/2018. |
| 15 | CL/147/2015 DC - Kantale | This action was instituted by a claimant claiming the articles seized by MBSL through Fiscal in the execution of writ in case no. HC/Civil/529/MR/2008. | Further inquiry on 22/05/2018. |
| 16 | CL/148/2015 DC - Kantale | This action was instituted by a claimant claiming the articles seized by MBSL through Fiscal in the execution of writ in case no. HC/Civil/529/MR/2008. | Respondent evidence to be lead on 22/05/2018. |
| 17 | CL/149/2015 DC - Kantale | This action was instituted by a claimant claiming the articles seized by MBSL through Fiscal in the execution of writ in case no. HC/Civil/529/MR/2008. | Respondent evidence to be lead on 22/05/2018. |

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|--|--|--|
| 18 | SC/HC/LA/43/2015 {HC/CIVIL496/09/ MR} | This Appeal was submitted by the Respondent/ Lessee in HC/Civil case no. 496/2009 the order of which was delivered in favour of MBSL by the High court. | Support on 03/09/2018. |
| 19 | 2963/L DC - Gampaha | Plaintiff filed this action seeking a declaration that the Mortgage Bond taken as security by MBSL be declared a nullity. | Order on 05/06/2018. |
| 20 | 6029/M DC - Gampaha | The Plaintiff has filed this action against the registered owner of the vehicle, the MBSL Insurance and MBSL seeking damages for injuries caused to the Plaintiff in an accident involving the above vehicle. MBSL is made a party since the absolute ownership of MBSL has still not been cancelled at the RMV despite being fully settled. According to the terms and conditions incorporated in the hire purchase agreement the liability falls entirely on the registered owner and the Insurer. | Answer for 1 defendant on 28/06/2018. |
| 21 | 7122/M DC - Kalutara | The Plaintiff has filed this action against the registered owner of the vehicle and the MBSL Insurance seeking damages for injuries caused to the Plaintiff in an accident involving the above vehicle. Although MBSL is made a party since the absolute ownership of MBSL has still not been cancelled at the RMV despite being fully settled. According to the terms and conditions incorporated in the Hire Purchase Agreement the liability falls entirely on the registered owner and the Insurer. It is important that no relief has been claimed from MBSL. | MBSL is the 4th defendant in this case. Learned district Judge discharged the Company from this case. Therefore no further date. |
| 22 | Claim -2 HC-Galle | This is a claim action arising from the execution of writ by MBSL in case no.HC/ARB/2193/2010. | Written submission on 16/05/2018. |
| 23 | Claim -3 HC-Galle | This is a claim action arising from the execution of writ by MBSL in case no.HC/ARB/2193/2010. | Written submission on 16/05/2018. |
| 24 | Claim -4 HC-Galle | This is a claim action arising from the execution of writ by MBSL in case no.HC/ARB/2193/2010. | Written submission on 16/05/2018. |
| 25 | DC Colombo 19426/L | Owner of the property denies the signature in the Mortgage Bond. | Case is laid by until identification of the heirs of the plaintiff. |
| 26 | DC Negombo 7300/L | Declaration of title sought by the Plaintiff. Judgment dated 04/11/2015 in favour of MBSL. The Plaintiff has appealed against the said judgement.(case no. HCCA/NEG/12/2015F) | Awaiting notice from Civil Appellate High Court of Negombo. |
| 27 | Mt. Lavinia 2357/07/L {L/18/08} DC Nugegoda 8/08 Connected to DC Col 17451/MB | Third party seeks a declaration of title on the property that was mortgaged to MBSL by the Borrower where judgment has been entered in favour of MBSL. | This case is laid by till the steps taken by the Plaintiff. |
| 28 | DC-Chilaw 4145/L | A third party seeks a declaration of title on the property that was mortgaged to MBSL and owned by MBSL through court auction. | Further trial on 07/05/2018. |
| 29 | DC-Kalutara 145/ PRO | Testamentary Action connected to DC Colombo case no.17513/MB {MBSL Vs D B Silva & M S M Fernando}. | Laid by until the substitution of the Petitioner. [Facility is fully settled] |

Notes to the Financial Statements

47 Contingent Liabilities and Commitments [Contd.]

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|------------------------------------|--|--|
| 30 | DC-Galle L/ 16855 | Third Party seeks a declaration of title in respect of the Property mortgaged to MBSL and owned by MBSL through court auction. | Further trial on 19/07/2018. |
| 31 | HC/ CIVIL/06/2013/MR | The Plaintiff is seeking, inter alia, the refund of the advance payment of Rs. 50,761,866.10 made by the Plaintiff to MBSL, in connection with a Share Sale and Purchase Agreement entered in March 2012 in respect of the sale of MBSL's shareholding in MBSL Savings Bank Limited at that time to a consortium of investors led by the Plaintiff and a Mandatory Injunction in this connection. Interim injunction refuse sought by the Plaintiff was refused. | Trial on 08/06/2018. |
| 32 | CHC/695/15/MR | The Plaintiff being a member of the consortium of investors who entered into a Share Transfer Agreement with MBSL in March 2012 with regard to the sale and purchase of MBSL's shareholding in MBSL Savings Bank Limited has instituted this action against MBSL, seeking the refund of the advance payment of Rs. 19,842,233.06 made by the Plaintiff to MBSL together with interest thereon at the rate of 25% per annum commencing from 28/03/2012 amounting to a total sum of Rs. 37,617,567 as at 27/10/2015. | Further trial on 02/04/2018 & 02/05/2018. |
| 33 | CA 198/07 HC[CIVIL] 145/98/1 | A Restitution - Integrum Action to set aside the judgment of Commercial High court dated 01.09.2003 which was in favour of MBSL and to set aside the Auction held on 17/01/2005. The Stay Order dated 29/03/2007 restraining MBSL from selling the land and premises was extended till the determination of this case of consent of both parties on 03/05/2007. | Application dismissed on 21/11/2017. However, the Petitioner has filed papers to vacate the said order. Support on 10/05/2018. |
| 34 | DSP/62/2015 DC - Colombo | The customer who has obtained a term loan facility from MBSL has filed this action seeking inter alia a declaration that they have to pay only another Rs. 3,321,489/- to settled the facility in full. Interim induction sought by the customer was refused. | Further Trial on 23/05/2018. |
| 35 | DC-Embilipitiya 9473/L | Plaintiff seeks a Declaration of Title on the property that was mortgaged to MBSL and owned by MBSL through court auction. | Case laid by till the final determination of the case no. 12941/ SPL filed against the Petitioner by a 3rd party. |
| 36 | 8190/L DC-Kurunegala | This action has been filed against MCSL Financial Services Limited (2nd Defendant) seeking a declaration of title for the land which has been mortgaged to MCSL Financial Services Limited by the 1st defendant. | Trem of Settlement Entered on 24/04/2017. |
| 37 | 826/L DC-Attanagalla | This action has been filed against MCSL Financial Services Limited (5th Defendant), seeking for an order declaring Mortgage Bond No1505 dated 16/11/2011 attested by J.C Ponnaiah, Notary Public and Deed of Tranfer null and void. | Further Trial on 07/08/2018. |
| 38 | 1520/MR/14 DC-Kaduwela | This action has been filed against MCSL Financial Services Limited (1st Defendant) and two others by a Customer of MCSL Financial Services Limited who has obtained a Lease Facility and defaulted. MCSL Financial Services Limited has been made a party to this action only for the notice purpose. | Trial on 28/05/2018. |

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|--|--|---|
| 39 | DMR/8867/09 DC-Colombo | The plaintiff filed action against MCSL Financial Services Limited seeking an order for damages caused to the plaintiff by wrongful conduct of the defendant. Judgment has been delivered in favour of MBSL - Appealed by Plaintiff. | On 01/04/2015, Order delivered in favour of MBSL- Civil Appellate case call on 27/07/2018 & 12/10/2018. |
| 40 | 8147/L DC-Kurunegala | Plaintiff has filed action against a Customer- (2nd Defendant) and MCSL Financial Services Limited (1st Defendant) seeking interim and permanent injunction orders restraining 1st Defendant from enforcing the Mortgage Bond No. 1825 dated 26/03/2011 attested by M.K.T.U Senevirathne, Notary Public. | Settlement on 29/06/2018. |
| 41 | DSP 98/10 DC-Colombo | The Plaintiff has filed action against MCSL Financial Services Limited (1st Defendant) and another person (2nd Defendant- Customer of Lease Facility) seeking a declaration that plaintiff is the owner of the land which has been mortgaged to MCSL Financial Services Limited. Judgment delivered in favour of MBSL . | On 25/04/2016 Judgment Delivered in favour of MBSL. Appeal filed by the Plaintiff. |
| 42 | DMR 608/12 DC-Colombo | Plaintiff has filed action against MCSL Financial Services Limited claiming damages for Malicious prosecution. | Written Submission on 2/05/2018. |
| 43 | 4977/SPL DC-Colombo | Plaintiff is seeking an order declaring Mortgage Bond No 77 dated 02-10-1995 attested by Mihirun Nisha Nachchiya Abdeen, Notary Public null and void. This case has been filed against MCSL Financial Services Limited and 3 others in 1997. | Further Trial on 15/06/2018. |
| 44 | 3114/L DC-Gampaha | This action has been filed against MCSL Financial Services Ltd (2nd Defendant) seeking declaration of title for the land which has been Mortgaged to MCSL Financial Services Ltd by the 1st Defendant. [Notice Only] | Replication on 13/06/2018. |
| 45 | 618/L DC-Kaduwela | This action has been filed against MCSL Financial Services Limited (2nd Defendant) seeking a decree restraining MBSL (2nd defendant) from dealing with the mortgage property to MCSL Financial Services Limited by the 1st Defendant until the determination of the inquiry pending before the Debt Conciliation Board. | Withdrawn the case on 23/02/2018. As this case has been settled in Debt Conciliation Board. |
| 46 | 00007/2016/DCL | Writ executed against 2D in the case no.1043/12/MR- In consequences of the execution of the writ Claim case has been filed by the petitioner in DC Colombo. | Inquiry on 18/05/2018. |
| 47 | DC/Matara/SPL/ 868 | This action has been filed challenging the repossession of a Vehicle regarding a Hire Purchase facility granted by MCSL Financial Services Limited. | Trial on 06/08/2018. |
| 48 | DSP 115/2016 DC-Colombo | This action has been instiuted by the Customer seeking a Restitutio integram order with regard to the Leased vehicle and an interim injunction restraining the Company from disposing the vehicle from the District Court of Colombo. | Trial on 04/07/2018. |
| 49 | CHC/215/2015/ MR [Commercial High Court] | Plaintiffs are the Shareholders of the company and they have filed an action in District Court of Colombo (case no. DMR/785/13) claiming Rs.3,841,000/- for the shares they have invested for amounting to Rs.2,400,000/-. This case has been transferred to the Commercial High Court by the District Court order dated 20.11.2015 considering the value of the case. | Trial on 26/06/2018. |

Notes to the Financial Statements

47 Contingent Liabilities and Commitments [Contd.]

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|--------------------------|---|---|
| 50 | LT/2/627/2016 | The applicant has filed this action in the Labour Tribunal of Colombo seeking an order for the reinstatement of his employment with back wages or in an alternative reasonable compensation against termination of his employment. | Further Trial on 12/06/2018. |
| 51 | LT/8/33/2016 | The Applicant has made an application to Labour Tribunal of Colombo seeking an order for the reinstatement of his employment with back wages or in an alternative reasonable compensation against the termination of his employment. | Further Trial on 14/05/2018 & 28/06/2018. |
| 52 | LT/01/ADDL/25/2016 | The applicant has sought an order for reinstatement of his employment with back wages and allowances or as an alternative reasonable compensation against the termination of his employment. | Further Inquiry on 22/05/2018. |
| 53 | LT/2/676/2016 | The applicant has filed this action in the Labour Tribunal of Colombo seeking an order for the reinstatement of his employment with back wages or in an alternative reasonable compensation against termination of his employment. | Further Trial on 12/06/2018. |
| 54 | 353/16/SPL | Plaintiff has filed this action against the Company and two others seeking nullity of several deeds in the title chain including the Mortgage Bond executed in favour of the bank and also claiming that the property alienated to the Company by way of Fiscal conveyance in subject to a constructive trust. | 1st Defendant steps by Plaintiff on 04/05/2018. |
| 55 | 322/SPL DC-Attagalla | This action has been filed seeking the release of the a property Mortgaged to MCSL following the settlement of all dues. The cancelled bond given to the customer has been lost/misplaced and MCSL has refused to issue a Deed of Release. No other relief sought. | Answer (1st, 2nd & 3rd) & Proxy for the 4th respondent on 29/06/2018. |
| 56 | DLA 8014/2007 DC-Negombo | This action has been filed by the Plaintiff against the Company and another in the District Court of Negombo seeking interim injunction preventing the Company auctioning the mortgage property executed in favour of the Company. Further the Plaintiff has sought to nullify the mortgage bond executed in favour of the Bank. | Answer (written Submission) on 24/05/2018. |
| 57 | DMR/01189/16 DC-Colombo | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing permanent disabilities to the Plaintiff' in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the Hire Purchase Agreement the liability falls entirely on the registered owner and the Insurer. | Pr-Trial on 24/05/2018. |
| 58 | 24931/M DC-Anuradhapura | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing permanent disabilities to the Plaintiff' in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the Lease Agreement the liability falls entirely on the registered owner and the Insurer. | Case was laid by the court [29/11/2017] - No further date. |

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|-----------------------------|---|-----------------------------------|
| 59 | DMR/00295/17 DC-Colombo | This action has been filed by an accident victim against the Registered Owner, the Driver, the Insurer and MBSL seeking damages for causing the death of the husband of the Plaintiff' in an accident involving the above vehicle. As the MBSL is the absolute owner the MBSL has been made a party to this action in accordance with the relevant legal provisions pertaining to the concept of vicarious liability. However as per the terms and conditions incorporated in the Lease Agreement the liability falls entirely on the registered owner and the Insurer. | Pre-Trial on 23/05/2018. |
| 60 | DC-KANDY DSP/00079/2016 | This an action filed by the Registered owner/lessee on the alleged failure of MBSL to handover the original of the certificate of registration to the registered owner and seeking a restraining order against the possible repossession of the vehicle by MBSL. However the position of MBSL is that the facility is not yet fully settled. | Answer on 05/06/2018. |
| 61 | DMR/1515/2017 DC-Colombo | This is an action instituted to secure a restraining order to prevent MBSL taking steps to repossess the Lease article and also to recover from MBSL the original of the certificate of registration thereto. However the MBSL has taken up the jurisdiction issue since this matter has to be heard at the arbitration and thereafter referred to the Commercial High Court of Colombo. | Written Submission on 04/05/2018. |
| 62 | 14363/SPL DC-Homagama | This is an action instituted by the Plaintiff seeking to have the mortgage bond executed in favour of MBSL as security for the facility declared a nullity, on the basis of a constructive trust. The matter is proceeding at the initial stages. | Written Submission on 22/05/2018. |
| 63 | 4016/M DC-Marawila | This is an action instituted by the Plaintiff seeking damages for wrongfully demanding a further sum of money despite the plaintiff alleged settlement of the facility. | Trial on 05/07/2018. |
| 64 | DC-GAMPAHA 3385/L | This is an action instituted by the Plaintiff seeking to have the mortgage bond executed in favour of MBSL as security for the facility declared a nullity, on the basis of a constructive trust. The matter is proceeding at the initial stages. | Answer on 28/06/2018. |
| 65 | 2093/L DC-Marawila | This is an action instituted by the Plaintiff seeking to have the mortgage bond executed in favour of MBSL as security for the facility declared a nullity on the basis that the plaintiff was not in a mentally fit and sound state at the time of execution of the mortgage bond. | Answer on 24/05/2018. |
| 66 | SC Appeal 26/2014 | This is a special leave to appeal sought by the UB Finance Company Ltd (formerly known as The Finance and Guarantee Ltd) against the Court of Appeal judgement dismissing its application for writ of Certiorari and Mandamus restraining the Commissioner of Labour effecting their decision that the UB Finance should deposit money amounting to a sum of Rs, 567,318/- In favour of a former employee of The Finance and Guarantee Ltd. MBSL had been named as a necessary party as MBSL was the Managing Agent of The Finance and Guarantee Ltd at that time. | Argument on 26/10/2018. |
| 67 | SC FR 207/17 | FR Application filed by a Depositor of The Finance and Guarantee Company Limited whose Deposit is converted to non-voting shares with his consent in accordance with Central Bank Directions. The Petitioner seeks a repayment plan for his Deposits/return for his shares. There is no claim against MBSL. MBSL has been made a party since MBSL had been managing the said entity during the period of the conversion to shares. | No claim against MBSL. |

Notes to the Financial Statements

47 Contingent Liabilities and Commitments [Contd.]

| No. | Action / Case No. | Purpose / Cause of Action | Position as at 27 April 2018 |
|-----|--|--|---|
| 68 | DC Gampaha 988/T Testamentary case regarding the facility provided to Lakmal Accessories (Pvt) Ltd. | Testamentary case filed with regard to the intestate estate of late Lalith Kumara Vithanage, who had been the owner of the property mortgaged to MBSL under this facility. Objections filed. | Order on 10/05/2018. |
| 69 | CHC/381/17/MR | The Plaintiff is seeking inter alia, damages from MBSL amounting to a sum of Rs. 9,000,000/- or such other sum to be determined by the court for cancellation of the Purchase Order dated 26/04/2016 in respect of the e-Financial Suit. [Core Leasing Software Solution] | Answer on 09/05/2018. |
| 70 | 000337/17/CL | Writ executed against 2D in the case no.1675/12/MR- In consequences of the execution of the writ Claim case has been filed by the petitioner against MBSL | Inquiry on 25/07/2018. |
| 71 | 3379/Land/ Gampaha | The Plaintiff had been the previous owner of a property which had been mortgaged to the Bank. This action has been filed on the basis that the alienation of the said property to the mortgagor is a forgery. Therefore the Plaintiff has sought a delaration nullifying the Deed of Gift executed in favour of the Mortgagor. In this matter the Bank has been named as the 3rd Defendant being the Mortgagee of the said property. | 1D & 2D - Summons Returnable, 3D - Answer on 19/07/2018. |
| 72 | 28394/Land / Avissawella | The subject property has been mortgaged to the Bank by the 1st Defendant to this action. Upon default the Bank has already filed a MB action bearing Case No.309/2014. The Plaintiff to this action alleged that the transfer executed in favour of the Mortgagor in respect of the subject property is a forgery. Therefore the Plaintiff has sought a nullity on both Deed of Transfer executed in the name of the 1st Defendant and the Mortgage Bond executed in favour of the Bank. | Summons Returnable on 01/06/2018. |

Group

47.2 Contingencies and commitments of MBSL Insurance Company Limited.

47.2.1 Contigent assets

The litigation initiated by the Subsidiary-MBSLI which is currently infavour to the subsidiary in the normal course of business are as follows:

- A litigation has been initiated by the Subsidiary-MBSLI against the Cricket Board of SriLanka to recover an unpaid premium of US \$ 619,158.

47.2.2 Contingent Liabilities

Litigation and claims which are currently against the subsidiary, MBSL Insurance Company Limited, in the normal course of business is summarized as follows:

| | 2017 Rs.'000 | 2016 Rs.'000 |
|--------------------|-----------------|-----------------|
| Bond claims | 47,599 | 4,899 |
| Insurance claims | 13,100 | 15,142 |
| Third party claims | 728,413 | 464,171 |
| | 789,112 | 484,212 |

48 Risk Management

Risk Management of the Company is the systematic process of identifying, quantifying and managing all risks and opportunities that can affect the achievement of the Merchant Bank of Sri Lanka & Finance PLC strategic and financial goals. Merchant Bank of Sri Lanka & Finance PLC has established a sound risk management framework to identify and mitigate the risk exposure.

The Board of Directors (BOD) is primarily responsible for overall risk management of Merchant Bank of Sri Lanka & Finance PLC. Hence the BOD has established Integrated Risk Management Committee for prudent risk management. Integrated Risk Management Committee (IRMC) of the company is responsible for:

- Assessing all risks that affect to Merchant Bank of Sri Lanka & Finance PLC and taking necessary actions to mitigate risks
- Reviewing the adequacy and effectiveness of all management level committees to address specific risks and managing those risks within quantitative risks limits identified by the committee.
- Assessing all aspects of risk management including updated business continuity plan
- Take prompt corrective actions to mitigate the effects of specific risks identified by the IRMC or Risk Management division

Merchant Bank of Sri Lanka & Finance PLC has identified 4 critical types of risk which can effect on MBSL's operations adversely as credit, market, liquidity and operational risks.

Risk Mitigation

Merchant Bank of Sri Lanka & Finance PLC has established IRMC, Assets and Liability Committee (ALCO), Investment and Credit Committees for mitigating the risk exposure, faced by the Company. Credit Committee is responsible to mitigate the credit risk while ALCO is responsible to mitigate the liquidity risk of Merchant Bank of Sri Lanka & Finance PLC by managing assets and liabilities of the Company. All the other committees report to the IRMC. The IRMC is responsible to manage the overall risk of Merchant Bank of Sri Lanka & Finance PLC and headed by a Board member. The Merchant Bank of Sri Lanka & Finance PLC uses accepted methods to mitigate risks faced by the Company.

Risk Measurement Systems

Merchant Bank of Sri Lanka & Finance PLC measures the expected and unexpected losses using various accepted models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. Merchant Bank of Sri Lanka & Finance PLC is developing exposure limits, forecasting, ratios and risk assessment forms to identify and measure the risk.

Credit Risk

Credit Risk is the potential that a company, borrower or counterparty will fail to meet its obligations in accordance with agreed terms. Financial Institutions need to manage the credit risk inherent in the entire portfolio as well as the risks associated with individual credits or transactions. Merchant Bank of Sri Lanka & Finance PLC has established a Credit Committee to ensure the credit quality of the Company. Credit Committee makes necessary amendments to collateral requirement, interest rates and exposure limits by analyzing credit worthiness of the counterparties. At present Merchant Bank of Sri Lanka & Finance PLC is in the process of developing a credit rating system to analyze the clientele. Exposure, Repayment capacity, Collateral value and purpose are used as criteria of credit ratings. Merchant Bank of Sri Lanka & Finance PLC analyzes the concentration to loan portfolio to mitigate the credit risk. Concentration is measured based on industry sector and geographical spread.

Concentration Risk

Concentration risk can arise from uneven distribution of exposures to its borrowers. Concentration risk can create in several ways:

- [a]. Individual counterparties
- [b]. Groups of individual counterparties or related entities
- [c]. Counterparties in specific geographical locations
- [d]. Industry sectors
- [e]. Specific products

Notes to the Financial Statements

48 Risk Management (Contd.)

Sector wise concentration and geographical concentration is considered to assess the concentration risk of the Company. Merchant Bank of Sri Lanka & Finance PLC focuses to maintain a diversified portfolio to reduce the concentration risk.

Market Risk

Market risk is the risk of losses in on and off balance sheet positions arising from movements in market prices. Market Risk can arise due to variations in interest rates, exchange rates, equity prices and commodity market prices. Interest rate risk and equity price risk mainly effect on Merchant Bank of Sri Lanka & Finance PLC business activities. Merchant Bank of Sri Lanka & Finance PLC uses sensitivity analysis, discounted cash flows and maturity gap analysis to calculate the market risk.

Liquidity Risk

Liquidity risk is the possibility of losses arising from fluctuations in Group's ability to sell or dispose the assets and settle the liabilities.

Groups believes that effective management of liquidity risk is vital for continuing Group's operations successful. Accordingly, Merchant Bank of Sri Lanka & Finance PLC has implemented the Board Approved Liquidity Risk Management Policy and established an Assets and Liability Committee (ALCO). Merchant Bank of Sri Lanka & Finance PLC uses ratios and maturity gap analysis to identify the liquidity risk of the Group.

Company

Industry Analysis Risk Concentration

The company's concentrations of risk are managed by industry sector.

| As at 31 December | Financial Services | Government | Consumers | Commercial Trading 1 | Agriculture | Diversified & Construction 2 | Transport & Tourism | Services 3 | Rs. '000 Total |
|---|--------------------|------------------|------------------|----------------------|-------------------|------------------------------|---------------------|------------------|-------------------|
| Financial Assets | | | | | | | | | |
| Cash and cash equivalents | 418,885 | - | - | - | - | - | - | - | 418,885 |
| Placements with banks & financial institutions | 1,509,597 | - | - | - | - | - | - | - | 1,509,597 |
| Securities purchased under resale agreements | - | 1,302,748 | - | - | - | - | - | - | 1,302,748 |
| Financial investments - held-for-trading | 116,238 | - | 3,150 | 19,726 | 1,410 | 52,951 | 36,566 | 1,223 | 231,264 |
| Bills receivable | 97,415 | - | - | 99,342 | - | 63,621 | 3,275 | 230,443 | 494,096 |
| Loans & advances to customers | 290,504 | - | 571,217 | 4,515,241 | 5,308,024 | 234,590 | 304,845 | 1,373,712 | 12,598,133 |
| Lease and hire purchase receivable | 132,267 | - | 904,082 | 5,838,331 | 6,372,376 | 253,263 | 586,909 | 1,574,204 | 15,661,432 |
| Financial investments - available-for-sale | | | | | | | | | |
| Government securities | - | 640,791 | - | - | - | - | - | - | 640,791 |
| Other securities | 1,260 | - | - | 26,500 | - | 23,794 | - | - | 51,554 |
| Unit Trust | 1,122,836 | - | - | - | - | - | - | - | 1,122,836 |
| Financial investments - held-to-maturity | 479,362 | - | - | - | - | - | - | - | 479,362 |
| Other assets | 46,865 | - | - | - | - | - | - | - | 46,865 |
| Total financial assets | 4,215,229 | 1,943,539 | 1,478,449 | 10,499,140 | 11,681,810 | 628,219 | 931,595 | 3,179,582 | 34,557,563 |

1 Commercial Trading includes Industry, Trade, Import & Export, Power, Retail and Wholesale and Margin Trading

2 Diversified & Construction includes Diversified Holdings, Manufacturing and Property Development

3 Services include IT, Health care, Telecommunication and others

Group

Industry Analysis Risk Concentration

The company's concentrations of risk are managed by industry sector.

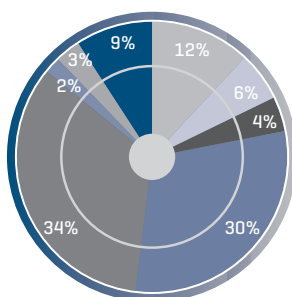
| As at 31 December | Financial Services | Government | Consumers | Commercial Trading 1 | Agriculture | Diversified & Construction 2 | Transport & Tourism | Services 3 | Total |
|---|--------------------|------------------|------------------|----------------------|-------------------|------------------------------|---------------------|------------------|-------------------|
| Rs. '000 | | | | | | | | | |
| Financial Assets | | | | | | | | | |
| Cash and cash equivalents | 466,139 | - | - | - | - | - | - | - | 466,139 |
| Placements with banks & financial institutions | 1,597,785 | - | - | - | - | - | - | - | 1,597,785 |
| Securities purchased under resale agreements | - | 1,651,927 | - | - | - | - | - | - | 1,651,927 |
| Financial investments - held-for-trading | 116,794 | - | 3,150 | 22,870 | 1,410 | 56,178 | 36,566 | 1,284 | 238,252 |
| Bills receivable | 97,415 | - | - | 99,342 | - | 63,621 | 3,275 | 230,443 | 494,096 |
| Loans & advances to customers | 213,053 | - | 571,217 | 4,587,515 | 5,308,024 | 234,590 | 304,845 | 1,373,712 | 12,592,956 |
| Lease and hire purchase receivable | 132,267 | - | 904,082 | 5,838,331 | 6,372,376 | 253,263 | 586,909 | 1,574,204 | 15,661,432 |
| Financial investments - available-for-sale | | | | | | | | | |
| Government securities | - | 978,638 | - | - | - | - | - | - | 978,638 |
| Other securities | 1,260 | - | - | 26,500 | - | 23,794 | - | - | 51,554 |
| Unit Trust | 1,161,650 | - | - | - | - | - | - | - | 1,161,650 |
| Financial investments - held-to-maturity | 479,362 | - | - | - | - | - | - | - | 479,362 |
| Other assets | 8,464 | - | - | 20,983 | - | 290 | - | 17,128 | 46,865 |
| Total financial assets | 4,274,189 | 2,630,565 | 1,478,449 | 10,595,541 | 11,681,810 | 631,736 | 931,595 | 3,196,771 | 35,420,656 |

1 Commercial Trading includes Industry, Trade, Import & Export, Power, Retail and Wholesale and Margin Trading

2 Diversified & Construction includes Diversified Holdings, Manufacturing and Property Development

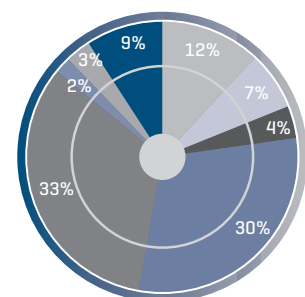
3 Services include IT, Health care, Telecommunication and others

2017 - Company



■ Financial Services ■ Government
■ Consumers ■ Commercial Trading 1
■ Agriculture ■ Diversified and Construction 2
■ Transport & Tourism ■ Services 3

2017 - Group



Notes to the Financial Statements

48 Risk Management (Contd.)

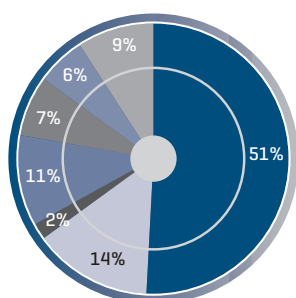
Geographical Analysis

The following table presents the distribution of financial assets of the Company & Group by geographical segment, allocated based on the location in which the financial assets and liabilities are recorded for the year ended 31 December 2017 together with comparative figures for the year ended 31 December 2016.

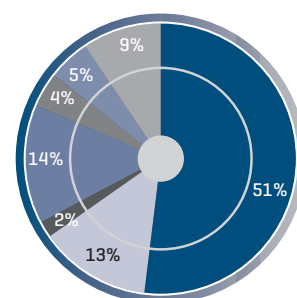
| Company As at 31 December | Western | | Southern & Sabaragamuwa | | Northern | |
|---|-------------------|-------------------|-------------------------|------------------|----------------|----------------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Financial Assets | | | | | | |
| Cash and cash equivalents | 320,513 | 256,279 | 28,211 | 43,381 | 5,143 | 12,513 |
| Placements with banks & financial institutions | 1,509,597 | 118,933 | - | - | - | - |
| Securities purchased under resale agreements | 1,302,748 | 265,687 | - | - | - | - |
| Financial investments - held-for-trading | 231,264 | 323,655 | - | - | - | - |
| Bills receivable | 355,913 | 618,092 | 43,426 | 37,846 | - | - |
| Loans and advances to customers | 6,514,137 | 6,552,287 | 2,392,758 | 1,829,056 | 308,820 | 405,410 |
| Lease and hire purchase receivable | 5,010,234 | 4,992,280 | 2,440,410 | 2,258,848 | 379,614 | 343,017 |
| Financial investments - available-for-sale | | | | | | |
| Government securities | 640,791 | 2,694,335 | - | - | - | - |
| Other securities | 1,174,390 | 41,310 | - | - | - | - |
| Financial investments - held-to-maturity | 479,362 | 57,766 | - | - | - | - |
| Other assets | 46,865 | 28,028 | - | 1,590 | - | 217 |
| Total financial assets | 17,585,814 | 15,948,652 | 4,904,805 | 4,170,721 | 693,577 | 761,157 |

| Group As at 31 December | Western | | Southern & Sabaragamuwa | | Northern | |
|---|-------------------|-------------------|-------------------------|------------------|----------------|----------------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Financial Assets | | | | | | |
| Cash and cash equivalents | 367,768 | 296,336 | 28,211 | 43,381 | 5,143 | 12,513 |
| Placements with banks & financial institutions | 1,597,785 | 262,319 | - | - | - | - |
| Securities purchased under resale agreements | 1,651,927 | 730,773 | - | - | - | - |
| Financial investments - held-for-trading | 238,252 | 331,586 | - | - | - | - |
| Bills receivable | 355,913 | 618,092 | 43,426 | 37,846 | - | - |
| Loans and advances to customers | 6,508,959 | 6,623,933 | 2,392,758 | 1,829,056 | 308,820 | 405,410 |
| Lease and hire purchase receivable | 5,010,234 | 4,992,280 | 2,440,410 | 2,258,848 | 379,614 | 343,017 |
| Financial investments - available-for-sale | | | | | | |
| Government securities | 978,638 | 3,049,945 | - | - | - | - |
| Other securities | 1,213,204 | 76,870 | - | - | - | - |
| Financial investments - held-to-maturity | 479,362 | 57,766 | - | - | - | - |
| Other assets | 46,865 | 28,028 | - | 1,590 | - | 217 |
| Total financial assets | 18,448,907 | 17,067,928 | 4,904,805 | 4,170,721 | 693,577 | 761,157 |

2017 - Company



2016 - Company



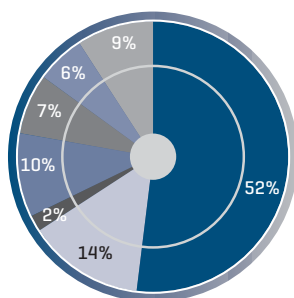
■ Western ■ Southern & Sabaragamuwa
■ Northern ■ North Western
■ North Central ■ Eastern & Uva
■ Central

Rs. '000

| North Western | | North Central | | Eastern & Uva | | Central | | Total | |
|---------------|-----------|---------------|-----------|---------------|-----------|-----------|-----------|------------|------------|
| 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| 23,722 | 36,738 | 8,993 | 11,478 | 12,792 | 17,953 | 19,509 | 22,957 | 418,885 | 401,301 |
| - | - | - | - | - | - | - | - | 1,509,597 | 118,933 |
| - | - | - | - | - | - | - | - | 1,302,748 | 265,687 |
| - | - | - | - | - | - | - | - | 231,264 | 323,655 |
| 48,313 | 31,256 | 312 | 7,292 | 11,615 | 9,816 | 34,517 | 35,102 | 494,096 | 739,403 |
| 734,157 | 910,958 | 636,523 | 204,131 | 960,630 | 577,442 | 1,051,109 | 841,561 | 12,598,133 | 11,320,845 |
| 2,871,010 | 3,323,026 | 1,749,512 | 1,064,820 | 1,146,444 | 1,004,498 | 2,064,207 | 2,005,261 | 15,661,432 | 14,991,751 |
| - | - | - | - | - | - | - | - | 640,791 | 2,694,335 |
| - | - | - | - | - | - | - | - | 1,174,390 | 41,310 |
| - | - | - | - | - | - | - | - | 479,362 | 57,766 |
| - | 2,539 | - | 245 | - | 433 | - | 1,402 | 46,865 | 34,454 |
| 3,677,202 | 4,304,517 | 2,395,340 | 1,287,966 | 2,131,482 | 1,610,142 | 3,169,343 | 2,906,283 | 34,557,563 | 30,989,440 |

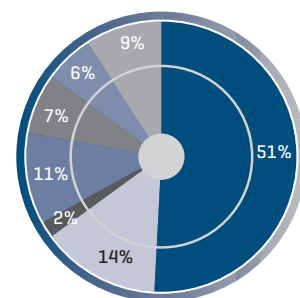
| North Western | | North Central | | Eastern & Uva | | Central | | Total | |
|---------------|-----------|---------------|-----------|---------------|-----------|-----------|-----------|------------|------------|
| 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| 23,722 | 36,738 | 8,993 | 11,478 | 12,792 | 17,953 | 19,509 | 22,957 | 466,139 | 441,357 |
| - | - | - | - | - | - | - | - | 1,597,785 | 262,319 |
| - | - | - | - | - | - | - | - | 1,651,927 | 730,773 |
| - | - | - | - | - | - | - | - | 238,252 | 331,586 |
| 48,313 | 31,256 | 312 | 7,292 | 11,615 | 9,816 | 34,517 | 35,102 | 494,096 | 739,403 |
| 734,157 | 910,958 | 636,523 | 204,131 | 960,630 | 577,442 | 1,051,109 | 841,561 | 12,592,956 | 11,392,491 |
| 2,871,010 | 3,323,026 | 1,749,512 | 1,064,820 | 1,146,444 | 1,004,498 | 2,064,207 | 2,005,261 | 15,661,432 | 14,991,751 |
| - | - | - | - | - | - | - | - | 978,638 | 3,049,945 |
| - | - | - | - | - | - | - | - | 1,213,204 | 76,870 |
| - | - | - | - | - | - | - | - | 479,362 | 57,766 |
| - | 2,539 | - | 245 | - | 433 | - | 1,402 | 46,865 | 34,454 |
| 3,677,202 | 4,304,517 | 2,395,340 | 1,287,966 | 2,131,482 | 1,610,142 | 3,169,343 | 2,906,283 | 35,420,656 | 32,108,715 |

2017 - Group



■ Western ■ Southern & Sabaragamuwa
■ Northern ■ North Western
■ North Central ■ Eastern & Uva
■ Central

2016 - Group



Notes to the Financial Statements

48 Risk Management (Contd.)

Maturity Analysis

The table below summarises the maturity portfolio of the undiscounted cash flows of the Group's financial assets and liabilities as at 31 December 2017.

Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the group could be required to be paid and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

| Maturity analysis | | | | | | | |
|--|------------------|------------------|------------------|-------------------|------------------|----------------|-------------------|
| Company | On Demand | Up to | 3 - 12 | 1-3 | 3-5 | More than | Total |
| | | 03 Months | Months | Years | Years | 5 Years | |
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| Assets | | | | | | | |
| Financial Assets | | | | | | | |
| Cash and cash equivalents | 418,885 | - | - | - | - | - | 418,885 |
| Placements with banks & financial institutions | 438,483 | 663,340 | 407,774 | - | - | - | 1,509,597 |
| Securities purchased under resale agreements | - | 797,033 | 505,715 | - | - | - | 1,302,748 |
| Financial investments - held-for-trading | - | 231,264 | - | - | - | - | 231,264 |
| Bills receivable | - | 494,096 | - | - | - | - | 494,096 |
| Loans and advances to customers | 66,239 | 1,676,285 | 3,392,007 | 4,878,139 | 2,128,146 | 457,317 | 12,598,133 |
| Lease and hire purchase receivable | 221,943 | 1,329,896 | 4,403,142 | 7,659,181 | 2,036,602 | 10,668 | 15,661,432 |
| Financial investments - available-for-sale | - | 1,122,836 | 343,878 | 100,957 | 195,956 | 51,554 | 1,815,181 |
| Financial investments - held-to-maturity | - | - | 420,165 | 57,696 | 1,501 | - | 479,362 |
| Financial other assets | - | 46,865 | - | - | - | - | 46,865 |
| Total financial assets | 1,145,550 | 6,361,615 | 9,472,681 | 12,695,973 | 4,362,205 | 519,539 | 34,557,563 |
| Non Financial Assets | | | | | | | |
| Real estate stock | - | - | 42,603 | - | - | - | 42,603 |
| Investment in associate company | - | - | - | - | - | 81,084 | 81,084 |
| Investment in subsidiary | - | - | - | - | - | 21,117 | 21,117 |
| Investment properties | - | - | - | - | - | 123,773 | 123,773 |

Maturity analysis

| Company | On Demand | Up to 03 Months | 3 - 12 Months | 1-3 Years | 3-5 Years | More than 5 Years | Total |
|----------------------------|------------------|--------------------|------------------|-------------------|------------------|----------------------|-------------------|
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| Property and equipment | - | - | - | - | - | 321,660 | 321,660 |
| Intangible assets | - | - | - | - | - | 226,293 | 226,293 |
| Other assets | - | 271,114 | - | - | - | - | 271,114 |
| Total non-financial assets | - | 271,114 | 42,603 | - | - | 773,927 | 1,087,644 |
| Total Assets | 1,145,550 | 6,632,729 | 9,515,284 | 12,695,973 | 4,362,205 | 1,293,466 | 35,645,207 |

Financial Liabilities

| | | | | | | | |
|---|------------------|-------------------|------------------|------------------|------------------|----------|-------------------|
| Due to banks | 123,849 | - | - | - | - | - | 123,849 |
| Securities sold under repurchase agreements | 437,672 | - | - | - | - | - | 437,672 |
| Due to customers | 485,594 | 8,553,996 | 8,462,870 | 2,644,843 | 1,771,566 | - | 21,918,869 |
| Debt issued and borrowed funds | 302,716 | 2,655,208 | 673,115 | 3,080,988 | 2,106,835 | - | 8,818,862 |
| Other financial liabilities | - | 338,072 | - | - | - | - | 338,072 |
| Total financial liabilities | 1,349,831 | 11,547,276 | 9,135,985 | 5,725,831 | 3,878,401 | - | 31,637,324 |

Non Financial Liabilities

| | | | | | | | |
|---------------------------------|------------------|-------------------|------------------|------------------|------------------|----------------|-------------------|
| Current tax liabilities | - | - | 7,473 | - | - | - | 7,473 |
| Deferred tax liabilities | - | - | - | - | - | 373,711 | 373,711 |
| Other liabilities | - | 129,893 | - | - | - | - | 129,893 |
| Retirement benefits obligations | - | - | - | - | - | 262,986 | 262,986 |
| Total Non financial liabilities | - | 129,893 | 7,473 | - | - | 636,697 | 774,063 |
| Total liabilities | 1,349,831 | 11,677,169 | 9,143,458 | 5,725,831 | 3,878,401 | 636,697 | 32,411,387 |

Equity

| | | | | | | | |
|-------------------------------------|------------------|-------------------|------------------|------------------|------------------|------------------|-------------------|
| Stated capital | - | - | - | - | - | 2,124,457 | 2,124,457 |
| Retained earnings | - | - | - | - | - | 924,947 | 924,947 |
| Available-for-sale reserve | - | 6,577 | - | - | - | - | 6,577 |
| Statutory reserves | - | - | - | - | - | 177,839 | 177,839 |
| Total equity | - | 6,577 | - | - | - | 3,227,243 | 3,233,820 |
| Total liabilities and equity | 1,349,831 | 11,683,746 | 9,143,458 | 5,725,831 | 3,878,401 | 3,863,940 | 35,645,207 |

Notes to the Financial Statements

48 Risk Management (Contd.)

Maturity Analysis

Maturity analysis

| Group | On Demand Rs.'000 | Up to 03 Months Rs.'000 | 3 - 12 Months Rs.'000 | 1-3 Years Rs.'000 | 3-5 Years Rs.'000 | More than 5 Years Rs.'000 | Total Rs.'000 |
|--|----------------------|-------------------------------|-----------------------------|-------------------------|-------------------------|---------------------------------|-------------------|
| Assets | | | | | | | |
| Financial Assets | | | | | | | |
| Cash and cash equivalents | 466,139 | - | - | - | - | - | 466,139 |
| Placements with banks & financial institutions | 438,483 | 663,340 | 495,962 | - | - | - | 1,597,785 |
| Securities purchased under resale agreements | - | 1,651,927 | - | - | - | - | 1,651,927 |
| Financial investments - held-for-trading | - | 238,252 | - | - | - | - | 238,252 |
| Bills receivable | - | 494,096 | - | - | - | - | 494,096 |
| Loans and advances to customers | 66,239 | 1,706,770 | 3,401,444 | 4,821,041 | 2,140,145 | 457,317 | 12,592,956 |
| Lease and hire purchase receivable | 221,943 | 1,329,896 | 4,403,142 | 7,659,181 | 2,036,602 | 10,668 | 15,661,432 |
| Financial investments - available-for-sale | - | 1,292,523 | 388,435 | 200,224 | 259,107 | 51,554 | 2,191,842 |
| Financial investments - held-to-maturity | - | - | 420,165 | 57,696 | 1,501 | - | 479,362 |
| Financial other assets | - | 46,865 | - | - | - | - | 46,865 |
| Total financial assets | 1,192,804 | 7,423,669 | 9,109,148 | 12,738,142 | 4,437,355 | 519,539 | 35,420,656 |
| Non Financial Assets | | | | | | | |
| Real estate stock | - | - | 42,603 | - | - | - | 42,603 |
| Investment in associate company | - | - | - | - | - | 92,453 | 92,453 |
| Investment properties | - | - | - | - | - | 123,773 | 123,773 |
| Property and equipment | - | - | - | - | - | 347,393 | 347,393 |
| Intangible assets | - | - | - | - | - | 244,526 | 244,526 |
| Other assets | - | 271,114 | 374,448 | - | - | - | 645,562 |
| Total non-financial assets | - | 271,114 | 417,051 | - | - | 808,145 | 1,496,310 |
| Total assets | 1,192,804 | 7,694,783 | 9,526,199 | 12,738,142 | 4,437,355 | 1,327,684 | 36,916,966 |

Maturity analysis

| Group | On Demand | Up to | 3 - 12 | 1-3 | 3-5 | More than | Total |
|---|----------------|----------------------|-------------------|------------------|------------------|--------------------|-------------------|
| | Rs.'000 | 03 Months Rs.'000 | Months Rs.'000 | Years Rs.'000 | Years Rs.'000 | 5 Years Rs.'000 | |
| Financial Liabilities | | | | | | | |
| Due to banks | 129,877 | - | - | - | - | - | 129,877 |
| Securities sold under repurchase agreements | - | 437,672 | - | - | - | - | 437,672 |
| Due to customers | 485,594 | 8,553,996 | 8,462,870 | 2,636,357 | 1,771,566 | - | 21,910,383 |
| Debt issued and borrowed funds | 302,716 | 2,655,208 | 673,115 | 3,080,988 | 2,106,835 | - | 8,818,862 |
| Other financial liabilities | - | 338,072 | - | - | - | - | 338,072 |
| Total financial liabilities | 918,187 | 11,984,948 | 9,135,985 | 5,717,345 | 3,878,401 | - | 31,634,866 |

Non Financial Liabilities

| | | | | | | | |
|---------------------------------|----------------|-------------------|-------------------|------------------|------------------|----------------|-------------------|
| Insurance provision - life | - | - | 547,026 | - | - | - | 547,026 |
| Insurance provision - non life | - | - | 430,093 | - | - | - | 430,093 |
| Current tax liabilities | - | - | 7,473 | - | - | - | 7,473 |
| Deferred tax liabilities | - | - | - | - | - | 373,711 | 373,711 |
| Other liabilities | - | 172,212 | 89,828 | 33,766 | 82,507 | 3,328 | 381,641 |
| Retirement benefits obligations | - | - | - | - | - | 283,000 | 283,000 |
| Total Non financial liabilities | - | 172,212 | 1,074,420 | 33,766 | 82,507 | 660,039 | 2,022,944 |
| Total liabilities | 918,187 | 12,157,160 | 10,210,405 | 5,751,111 | 3,960,908 | 660,039 | 33,657,810 |

Equity

| | | | | | | | |
|-------------------------------------|----------------|-------------------|-------------------|------------------|------------------|------------------|-------------------|
| Stated capital | - | - | - | - | - | 2,124,457 | 2,124,457 |
| Retained earnings | - | - | - | - | - | 948,415 | 948,415 |
| Available-for-sale reserve | - | 6,577 | - | - | - | (5,277) | 1,300 |
| Statutory reserves | - | - | - | - | - | 177,839 | 177,839 |
| Non controlling interests | - | - | - | - | - | 7,145 | 7,145 |
| Total equity | - | 6,577 | - | - | - | 3,252,579 | 3,259,156 |
| Total liabilities and equity | 918,187 | 12,163,737 | 10,210,405 | 5,751,511 | 3,960,908 | 3,912,618 | 36,916,966 |

Notes to the Financial Statements

48 Risk Management (Contd.)

Maturity of the Group's Contingent Liabilities and Commitments

The table below shows the contractual expiry by maturity of the Group's contingent liabilities and commitments.

For issued guarantees to customers the maximum amount of the guarantees is allocated to the earliest period in which the guarantee could be called.

| | On Demand | Less than 3 Months | 3 - 12 Months | 1-3 Years | 3-5 Years | Over 5 Years | Rs.'000 Total as at 31-12-2017 |
|--|-----------|-----------------------|------------------|--------------|--------------|-----------------|--------------------------------------|
| Company | | | | | | | |
| Financial Guarantees & Claims to the customers | 167,712 | - | - | - | - | - | 167,712 |
| Total commitments and contingencies | 167,712 | - | - | - | - | - | 167,712 |

| | On Demand | Less than 3 Months | 3 - 12 Months | 1-3 Years | 3-5 Years | Over 5 Years | Rs.'000 Total as at 31-12-2017 |
|--|-----------|-----------------------|------------------|--------------|--------------|-----------------|--------------------------------------|
| Group | | | | | | | |
| Financial Guarantees & Claims to the customers | 183,166 | - | - | - | - | - | 183,166 |
| Total commitments and contingencies | 183,166 | - | - | - | - | - | 183,166 |

The Group expects that not all the contingent liabilities and commitments will be drawn before expiry of the commitments.

Impairment Assessment

Group uses an incurred loss model for the recognition of losses on impaired financial assets. Therefore, losses can only be recognised when objective evidence of a specific loss event has been observed. Triggering events include the following:

- * Significant financial difficulty of the customer
- * A breach of contract such as a default of payment
- * Where the company grants a customer a concession due to the customer experiencing financial difficulty
- * It becomes probable that the customer will enter bankruptcy or other financial reorganization
- * Internal or external observable data that suggests that there is a decrease in the estimated future cash flows from the loans

This approach differs from the direction issued by the Central Bank of Sri Lanka.

Individually Assessed Allowances

Merchant Bank of Sri Lanka & Finance PLC assesses the impairment allowances for each individually significant loan or advance on an individual basis, include any overdue payments of interests, breaching of the debt covenant or credit rating downgrades. Items considered when determining allowance amounts include projected receipts and the expected payout should bankruptcy ensue, the counterparty's business plan, availability of financial support to the counter party, realizable value of the collateral and the timing of the expected cash flows. Merchant Bank of Sri Lanka & Finance PLC assesses the impairment allowances at each reporting date, unless unexpected negative circumstances require more attention.

48 Risk Management (Contd.)

Collectively Assessed Allowances

Merchant Bank of Sri Lanka & Finance PLC assesses the impairment allowance for loans and advances and held to maturity debt instruments that are not individually significant and for individually significant loans and advances that have been assessed individually and determined not to be impaired. The collective assessment is computed for groups of lending assets with similar risk characteristics and Merchant Bank of Sri Lanka & Finance PLC assesses the collective allowances based on historical information.

As at 31 December 2017 the value of collateral that the company holds relating to loans individually determined to be impaired amounts to Rs. 1,656 Mn. The collateral consists of cash, securities and properties.

Credit Quality by class of financial assets

The table below shows the credit quality by class of assets for all financial assets exposed to credit risk.

| Company | Neither Past Due nor Impaired* | Past due but not impaired * | | | | | Individually Impaired | Total as at 31-12-2017 |
|---|--------------------------------------|-----------------------------|------------------|------------------|-------------------|------------------|--------------------------|---------------------------|
| | | Less than 3 Months | 3 to 6 Months | 6 to 9 Months | 9 to 12 Months | More than 12 | | |
| Financial Assets | | | | | | | | |
| Cash and cash equivalents | 418,885 | - | - | - | - | - | - | 418,885 |
| Placements with banks & financial institutions | 1,509,597 | - | - | - | - | - | - | 1,509,597 |
| Securities purchased under resale agreements | 1,302,748 | - | - | - | - | - | - | 1,302,748 |
| Financial investments - held-for-trading | 231,264 | - | - | - | - | - | - | 231,264 |
| Bills receivable | 120,713 | - | 20,832 | 32,832 | - | 96,925 | 357,203 | 628,505 |
| Loans and advances to customers | 5,865,638 | 2,219,781 | 1,533,100 | 529,568 | 552,532 | 1,351,915 | 1,294,271 | 13,346,805 |
| Lease and hire purchase receivable | 8,499,073 | 4,006,582 | 2,135,857 | 66,294 | 134,522 | 763,064 | 453,647 | 16,059,040 |
| Financial investments - available-for-sale | | | | | | | | |
| Government securities | 640,791 | - | - | - | - | - | - | 640,791 |
| Other securities | 51,554 | - | - | - | - | - | - | 51,554 |
| Financial investments - held-to-maturity | 479,362 | - | - | - | - | - | - | 479,362 |
| Unit trust | 1,122,836 | - | - | - | - | - | - | 1,122,836 |
| Other assets | 46,865 | - | - | - | - | - | - | 46,865 |
| Total | 20,289,327 | 6,226,363 | 3,689,789 | 628,694 | 687,054 | 2,211,904 | 2,105,121 | 35,838,252 |

Notes to the Financial Statements

Risk Management (Contd.)

| Group | Neither Past Due nor Impaired* | Past due but not impaired * | | | | | Individually Impaired | Total as at 31-12-2017 |
|---|--------------------------------------|-----------------------------|------------------|------------------|-------------------|------------------|--------------------------|---------------------------|
| | | Less than 3 Months | 3 to 6 Months | 6 to 9 Months | 9 to 12 Months | More than 12 | | |
| Financial Assets | | | | | | | | |
| Cash and cash equivalents | 466,139 | - | - | - | - | - | - | 466,139 |
| Placements with banks & financial institutions | 1,597,785 | - | - | - | - | - | - | 1,597,785 |
| Securities purchased under resale agreements | 1,651,927 | - | - | - | - | - | - | 1,651,927 |
| Financial investments - held-for-trading | 238,252 | - | - | - | - | - | - | 238,252 |
| Bills receivable | 120,713 | - | 20,832 | 32,832 | - | 96,925 | 357,203 | 628,505 |
| Loans and advances to customers | 5,860,461 | 2,219,781 | 1,533,100 | 529,568 | 552,532 | 1,351,915 | 1,294,271 | 13,341,628 |
| Lease and hire purchase receivable | 8,499,073 | 4,006,582 | 2,135,857 | 66,294 | 134,522 | 763,064 | 453,647 | 16,059,039 |
| Financial investments - available-for-sale | | | | | | | | |
| Government securities | 978,638 | - | - | - | - | - | - | 978,638 |
| Other securities | 51,554 | - | - | - | - | - | - | 51,554 |
| Financial investments - held-to-maturity | 479,362 | - | - | - | - | - | - | 479,362 |
| Unit trust | 1,161,650 | - | - | - | - | - | - | 1,161,650 |
| Other assets | 46,865 | - | - | - | - | - | - | 46,865 |
| Total | 21,152,419 | 6,226,363 | 3,689,789 | 628,694 | 687,054 | 2,211,904 | 2,105,121 | 36,701,344 |

* Collective impairment allowances are made for 'neither past due nor impaired' and 'past due but not impaired' loans.

48 Operational risk

Operational risk refers to the risk that risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk includes legal risk, but excludes strategic and reputational risk. Group's Integrated Risk Management Committee and Risk Management division has taken necessary actions to identify and manage the company operational risk prudently and effectively.

The company recognises that operational risk is inherent in all business activities and can bring unprecedented losses or damages to its business through direct or indirect financial loss, brand or reputational damage, customer dissatisfaction, legal or regulatory penalties if such risks are not objectively managed.

49 Capital

The company maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the company’s capital is monitored using, among other measures, the rules and ratios established by the Central Bank of Sri Lanka.

During the past year, the company had complied in full with all its externally imposed capital requirements. [2016: the same].

Capital Management

The primary objectives of the company’s capital management policy are to ensure that the company complies with externally imposed capital requirements and that the company maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholder value.

The company manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the company may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes yet have been made in the objectives, policies and processes from the previous years, however, it is under constant scrutiny of the Board.

Capital Adequacy Ratio [CAR]

The company’s CAR remained well above the minimum ratio prescribed by the CBSL despite substantial increase in loans and advances.

| Month | Core Capital Ratio [%] 2017 | Core Capital Ratio [%] 2016 | Total Capital Ratio [%] 2017 | Total Capital Ratio [%] 2016 |
|--------|---------------------------------------|--------------------------------|--|---------------------------------|
| 31-Mar | 10.33 | 11.75 | 10.38 | 11.63 |
| 30-Jun | 10.49 | 11.35 | 15.70 | 11.24 |
| 30-Sep | 10.48 | 11.10 | 15.68 | 11.07 |
| 31-Dec | 10.21 | 10.66 | 15.27 | 10.69 |

Supplementary Information

Quarterly Analysis

Statement of Profit or Loss

| | 1st Quarter | | 2nd Quarter | | 3rd Quarter | | 4th Quarter | | Total | |
|---|-------------|-----------|-------------|-----------|-------------|-----------|-------------|-----------|-----------|-----------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Income | 1,392,757 | 1,036,131 | 1,642,428 | 1,162,119 | 1,648,551 | 1,271,441 | 1,719,089 | 1,418,464 | 6,402,825 | 4,888,155 |
| Interest and similar income | 1,352,822 | 1,077,704 | 1,541,704 | 1,098,172 | 1,600,942 | 1,202,326 | 1,661,818 | 1,359,572 | 6,157,286 | 4,737,774 |
| Interest and similar expenses | 834,988 | 585,476 | 927,858 | 629,462 | 967,963 | 711,596 | 977,999 | 783,070 | 3,708,808 | 2,709,604 |
| Net interest income | 517,834 | 492,228 | 613,846 | 468,710 | 632,979 | 490,730 | 683,819 | 576,502 | 2,448,478 | 2,028,170 |
| Fee and commission income | 13,004 | 8,858 | 43,279 | 33,833 | 32,458 | 32,093 | 90,946 | 56,699 | 179,687 | 131,483 |
| Fee and commission expenses | - | - | 36,689 | 20,217 | 13,680 | 16,244 | 9,595 | 1,352 | 59,964 | 37,813 |
| Net fee and commission income | 13,004 | 8,858 | 6,590 | 13,616 | 18,778 | 15,849 | 81,351 | 55,347 | 119,723 | 93,670 |
| Net trading income | (3,047) | 4,352 | (14,925) | 6,136 | 1,324 | (32,662) | 630 | 32,246 | (16,018) | 10,072 |
| Net gain / (loss) on financial assets - held for trading | (18,309) | (90,416) | 49,929 | 16,524 | (17,074) | 65,715 | (8,922) | (52,919) | 5,624 | (61,096) |
| Other operating income | 48,287 | 35,633 | 22,441 | 7,454 | 30,901 | 3,969 | (25,383) | 22,866 | 76,246 | 69,922 |
| Total operating income | 557,769 | 450,655 | 677,881 | 512,440 | 666,908 | 543,601 | 731,495 | 634,042 | 2,634,053 | 2,140,738 |
| Impairment charges from loans and other losses | (11,448) | 14,368 | 27,407 | (15,665) | 182,312 | (511) | 45,960 | 26,047 | 244,231 | 24,239 |
| Net operating income | 569,217 | 436,287 | 650,474 | 528,105 | 484,596 | 544,112 | 685,535 | 607,995 | 2,389,822 | 2,116,499 |
| Personnel expenses | 242,094 | 180,916 | 278,145 | 190,954 | 282,500 | 187,909 | 224,353 | 221,751 | 1,027,092 | 781,530 |
| Provision for employee benefit | 11,087 | 12,000 | 11,088 | 12,000 | 11,087 | 12,000 | 13,172 | 4,464 | 46,434 | 40,464 |
| Depreciation of property & equipment | 20,258 | 14,974 | 20,324 | 14,644 | 20,693 | 15,099 | 20,869 | 19,691 | 82,144 | 64,408 |
| Amortisation of intangible assets | 3,655 | 3,245 | 3,603 | 3,222 | 9,993 | 3,502 | 9,630 | 670 | 26,881 | 10,639 |
| Other operating expenses | 189,197 | 158,221 | 160,831 | 144,577 | 191,485 | 168,612 | 201,516 | 170,530 | 743,029 | 641,940 |
| Total operating expense | 466,291 | 369,356 | 473,991 | 365,397 | 515,758 | 387,122 | 469,540 | 417,106 | 1,925,580 | 1,538,981 |
| Profit / (loss) from operations | 102,926 | 66,931 | 176,483 | 162,708 | (31,162) | 156,990 | 215,995 | 190,889 | 464,242 | 577,518 |
| Impairment from investment in Group companies | - | - | - | - | - | - | 56,189 | 232,891 | 56,189 | 232,891 |
| Profit / (loss) from operations after impairment from subsidiary investments | 102,926 | 66,931 | 176,483 | 162,708 | (31,162) | 156,990 | 159,806 | (42,002) | 408,053 | 344,627 |
| Value added tax (VAT) on financial services | 40,669 | 19,780 | 44,414 | 36,246 | 45,226 | 25,345 | 49,094 | 30,359 | 179,403 | 111,730 |
| Profit before income tax | 62,257 | 47,151 | 132,069 | 126,462 | (76,388) | 131,645 | 110,712 | (72,361) | 228,650 | 232,897 |
| Income tax expense | 12,394 | 9,812 | 29,523 | 28,758 | (17,461) | 9,332 | 103,343 | 106,345 | 127,799 | 154,247 |
| Profit/(loss) for the period | 49,863 | 37,339 | 102,546 | 97,704 | (58,927) | 122,313 | 7,369 | (178,706) | 100,851 | 78,650 |

Quarterly Analysis

Statement of Financial Position

| As at | 1st Quarter | | 2nd Quarter | | 3rd Quarter | | 4th Quarter | |
|--|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Assets | | | | | | | | |
| Cash and cash equivalents | 353,144 | 388,947 | 306,797 | 321,913 | 448,252 | 392,636 | 418,885 | 401,301 |
| Placements with banks & financial institutions | 100,544 | 445,694 | 945,206 | - | 1,023,105 | 114,680 | 1,509,597 | 118,933 |
| Securities purchased under resale agreements | 272,134 | 641,941 | 1,375,943 | 402,539 | 2,884,148 | 259,097 | 1,302,748 | 265,687 |
| Financial investments-held-for-trading | 249,352 | 450,180 | 214,398 | 412,827 | 220,481 | 365,208 | 231,264 | 323,655 |
| Bills receivable | 713,252 | 567,313 | 764,814 | 602,008 | 739,803 | 636,514 | 494,096 | 739,403 |
| Loans and advances to customers | 12,171,032 | 8,867,925 | 13,011,700 | 9,552,434 | 12,902,197 | 10,290,565 | 12,598,133 | 11,320,845 |
| Lease and hire purchase rental receivable | 15,423,304 | 14,576,853 | 15,983,943 | 15,104,138 | 15,577,769 | 14,963,546 | 15,661,432 | 14,991,751 |
| Financial investments-available-for-sale | 2,783,619 | 1,921,816 | 1,797,573 | 2,399,070 | 665,970 | 2,684,048 | 1,815,181 | 2,735,645 |
| Financial investments-held-to-maturity | 59,374 | 58,082 | 257,283 | 57,221 | 481,784 | 56,596 | 479,362 | 57,766 |
| Real Estate Stock | 19,188 | 40,788 | 52,019 | 30,826 | 53,245 | 28,844 | 42,603 | 24,144 |
| Investments in associate companies | 81,084 | 81,084 | 81,084 | 81,084 | 81,084 | 81,084 | 81,084 | 81,084 |
| Investments in subsidiaries | 77,306 | 310,197 | 77,306 | 310,197 | 77,306 | 310,197 | 21,117 | 77,306 |
| Investment properties | 125,953 | 145,081 | 125,226 | 139,073 | 124,500 | 138,347 | 123,773 | 127,670 |
| Property and equipment | 301,313 | 216,805 | 300,612 | 206,296 | 337,909 | 231,779 | 321,660 | 312,337 |
| Intangible assets | 34,050 | 36,174 | 30,954 | 32,996 | 233,908 | 41,597 | 226,293 | 37,705 |
| Other assets | 392,985 | 222,927 | 442,961 | 316,406 | 309,074 | 331,265 | 317,979 | 318,496 |
| Total assets | 33,157,634 | 28,971,807 | 35,767,819 | 29,969,028 | 36,160,535 | 30,926,003 | 35,645,207 | 31,933,728 |
| Liabilities | | | | | | | | |
| Due to banks | 549,775 | 132,888 | 211,560 | 445,193 | 283,433 | 220,408 | 123,849 | 201,635 |
| Securities sold under repurchase agreements | 383,332 | 401,064 | 421,175 | 403,808 | - | 401,125 | 437,672 | 401,820 |
| Due to customers | 19,060,077 | 18,014,561 | 21,027,326 | 17,169,383 | 22,757,385 | 17,748,712 | 21,918,869 | 18,518,419 |
| Debt issued and borrowed funds | 9,092,037 | 6,543,438 | 9,550,577 | 7,915,018 | 8,656,616 | 8,383,712 | 8,818,862 | 8,722,787 |
| Current tax liabilities | 144,081 | 143,422 | 161,430 | 172,180 | 131,879 | 171,612 | 7,473 | 151,128 |
| Deferred tax liabilities | 206,888 | 113,669 | 213,455 | 113,669 | 206,888 | 113,669 | 373,711 | 206,888 |
| Other liabilities | 339,832 | 374,662 | 688,495 | 408,933 | 665,668 | 389,086 | 467,965 | 404,174 |
| Employee benefit liability | 223,832 | 257,278 | 224,784 | 255,796 | 235,214 | 254,811 | 262,986 | 213,388 |
| Total liabilities | 29,999,854 | 25,980,982 | 32,498,802 | 26,883,980 | 32,937,083 | 27,683,135 | 32,411,387 | 28,820,239 |
| Equity | | | | | | | | |
| Stated capital | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 |
| Retained profits | 903,028 | 771,834 | 1,005,574 | 869,538 | 946,636 | 991,851 | 177,839 | 157,669 |
| Available-for-sale reserve | (27,374) | (46,010) | (18,683) | (49,491) | (5,310) | (13,984) | 924,947 | 853,165 |
| Statutory reserves | 157,669 | 140,544 | 157,669 | 140,544 | 157,669 | 140,544 | 6,577 | (21,802) |
| Total equity | 3,157,780 | 2,990,825 | 3,269,017 | 3,085,048 | 3,223,452 | 3,242,868 | 3,233,820 | 3,113,489 |
| Total liabilities and equity | 33,157,634 | 28,971,807 | 35,767,819 | 29,969,028 | 36,160,535 | 30,926,003 | 35,645,207 | 31,933,728 |

Decade at a Glance

Based on Financial Statements Prepared in Compliance with SLAS

| For the year ended 31 December | Company | | | Group | | |
|--|------------------|------------------|------------------|-------------------|-------------------|------------------|
| | 2010 Rs.'000 | 2009 Rs.'000 | 2008 Rs.'000 | 2010 Rs.'000 | 2009 Rs.'000 | 2008 Rs.'000 |
| Operating Results | | | | | | |
| Income | 1,522,980 | 1,155,731 | 1,035,227 | 2,595,680 | 2,332,321 | 1,647,537 |
| Interest expenses | 419,041 | 584,247 | 547,386 | 850,177 | 1,274,896 | 921,486 |
| Net interest income | 688,080 | 398,298 | 419,918 | 1,080,630 | 720,752 | 628,435 |
| Operating expenses & provisions | 535,870 | 345,720 | 300,898 | 1,032,534 | 727,000 | 494,628 |
| Share of associate company | 82,639 | 28,500 | 16,471 | 82,639 | 28,500 | 16,471 |
| Profit before income tax | 650,708 | 254,264 | 203,414 | 795,608 | 358,925 | 247,894 |
| Income tax on profit | 201,037 | 53,286 | [1,664] | 233,700 | 73,592 | 4,908 |
| Profit after income tax | 449,671 | 200,978 | 205,078 | 540,977 | 285,333 | 242,986 |
| Minority interest | - | - | - | 48,632 | 55,771 | 18,574 |
| Net profit attributable to equity holders of the Parent | 449,671 | 200,978 | 205,078 | 492,345 | 229,562 | 224,412 |
| Balance Sheet Information | | | | | | |
| Assets | | | | | | |
| Government treasury bills and bonds | 279,765 | 387,847 | 131,084 | 1,626,575 | 1,291,653 | 446,084 |
| Investments on securities & others | 622,900 | 511,217 | 395,616 | 892,052 | 768,975 | 430,929 |
| Loans and advances | 1,567,034 | 1,143,361 | 807,469 | 3,960,576 | 3,435,815 | 1,672,491 |
| Lease receivable | 3,816,504 | 2,958,996 | 3,128,124 | 6,554,698 | 5,035,167 | 4,660,299 |
| Property, plant & equipment | 44,047 | 37,844 | 30,519 | 145,426 | 150,924 | 44,466 |
| Investments in associate & subsidiary companies | 568,327 | 354,546 | 103,895 | 121,617 | 95,022 | 82,977 |
| Other assets | 284,024 | 185,114 | 171,421 | 1,123,406 | 1,054,916 | 251,782 |
| Total assets | 7,182,601 | 5,578,925 | 4,768,128 | 14,424,350 | 11,832,472 | 7,589,028 |
| Liabilities | | | | | | |
| Deposits from customers | - | - | - | 5,676,955 | 4,897,367 | 2,199,270 |
| Debentures | 716,800 | 1,074,160 | 1,144,160 | 734,684 | 1,169,644 | 1,144,160 |
| Borrowings | 3,179,712 | 1,658,985 | 1,553,949 | 3,311,089 | 1,733,170 | 1,682,372 |
| Other liabilities & deferred taxation | 606,896 | 515,008 | 390,225 | 1,514,540 | 1,307,202 | 553,314 |
| | 4,503,408 | 3,248,153 | 3,088,334 | 11,237,268 | 9,107,383 | 5,579,116 |
| Minority interest | - | - | - | 288,683 | 207,823 | 172,208 |
| Net assets | 2,679,193 | 2,330,772 | 1,679,794 | 2,898,399 | 2,517,266 | 1,837,704 |
| Capital Employed | | | | | | |
| Stated capital | 1,607,000 | 1,607,000 | 1,067,000 | 1,607,000 | 1,607,000 | 1,067,000 |
| Retained profit/[loss] & reserve fund | 1,072,193 | 723,772 | 612,794 | 1,291,399 | 910,266 | 770,704 |
| | 2,679,193 | 2,330,772 | 1,679,794 | 2,898,399 | 2,517,266 | 1,837,704 |

Decade at a Glance

Ratios and Related Information

| For the year ended 31 December | Company | | | Group | | |
|--------------------------------------|---------|--------|---------|-------|-------|---------|
| | 2010 | 2009 | 2008 | 2010 | 2009 | 2008 |
| Operating Ratios | | | | | | |
| Return on Net Assets - % | 16.78 | 8.62 | 12.21 | 16.99 | 9.12 | 12.21 |
| Net Profit - % | 29.53 | 17.39 | 19.81 | 20.84 | 12.23 | 14.75 |
| Net Interest Margin - % | 13.55 | 9.31 | 10.72 | 2.47 | 2.18 | 2.45 |
| Cost to Income Ratio - % | 42.58 | 54.95 | 53.30 | 52.50 | 70.44 | 55.15 |
| Income Growth - % | 31.78 | 11.64 | 18.64 | 11.29 | 41.56 | 14.10 |
| Profit Growth - % | 123.74 | (2.00) | (14.00) | 96.93 | 17.43 | (16.05) |
| Assets Growth - % | 28.75 | 17.00 | 8.27 | 21.90 | 55.92 | 11.56 |
| Net Assets Growth - % | 14.95 | 38.75 | 7.35 | 15.14 | 36.98 | 7.89 |
| Gearing Ratios | | | | | | |
| Debt to Equity - Times | 1.45 | 1.17 | 1.61 | 3.34 | 3.10 | 2.73 |
| Interest Cover - Times | 2.55 | 1.44 | 1.37 | 1.94 | 1.28 | 1.27 |
| Liquidity Ratios | | | | | | |
| Quick Ratio - Times | 0.93 | 1.04 | 1.19 | 0.69 | 0.85 | 0.87 |
| Investors Ratios | | | | | | |
| Market value of a voting share - Rs. | 45.80 | 19.50 | 7.25 | 45.80 | 19.50 | 7.25 |
| Basic Earnings Per Share - Rs. | 3.33 | 1.49 | 2.28 | 3.65 | 1.70 | 2.49 |
| Net Assets Value Per Share - Rs. | 19.85 | 17.26 | 18.66 | 21.47 | 18.65 | 20.42 |
| Price Earnings Ratio - Times | 13.75 | 13.09 | 3.18 | 12.55 | 11.47 | 2.91 |
| Earning Yield - % | 7.27 | 7.64 | 31.45 | 7.97 | 8.72 | 34.34 |
| Dividend Per Share - Rs. | 1.25 | 0.75 | 1.00 | 1.25 | 0.75 | 1.00 |
| Dividend Cover - Times | 2.66 | 1.98 | 2.28 | 2.92 | 2.27 | 2.49 |
| Dividend Yield Ratio - % | 2.73 | 3.85 | 13.79 | 2.73 | 3.85 | 13.79 |
| Dividend Payout Ratio - % | 37.54 | 50.34 | 43.86 | 34.25 | 44.12 | 40.16 |

Based on Financial Statements Prepared Under SLFRS

| For the year ended 31 December | Company | | | | | | |
|---|------------------------|-----------------------------|-------------------|-----------------------------|-------------------|-------------------|------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2015 Rs.'000 | 2014 Rs.'000 Restated | 2013 Rs.'000 | 2012 Rs.'000 | 2011 Rs.'000 |
| Operating Results | | | | | | | |
| Income | 6,402,825 | 4,888,155 | 4,216,991 | 4,734,641 | 2,355,366 | 1,869,714 | 1,393,526 |
| Interest expenses | 3,708,808 | 2,709,604 | 2,133,325 | 2,579,431 | 1,371,937 | 1,035,739 | 541,370 |
| Net interest income | 2,448,478 | 2,028,170 | 1,939,834 | 1,805,198 | 893,899 | 779,559 | 782,407 |
| Operating expenses & provisions | 2,465,367 | 1,945,654 | 2,119,094 | 2,101,923 | 807,547 | 590,572 | 483,141 |
| Share of associate company | - | - | - | - | - | - | 60,248 |
| Profit before income tax | 228,650 | 232,897 | [35,428] | 53,287 | 175,882 | 243,403 | 429,263 |
| Income tax on profit | 127,799 | 154,247 | 42,878 | 83,957 | 58,942 | 42,156 | 92,992 |
| Profit after income tax | 100,851 | 78,650 | [78,306] | [30,670] | 116,940 | 201,247 | 336,271 |
| Non controlling interests | - | - | - | - | - | - | - |
| Net profit attributable to equity holders of the Parent | 100,851 | 78,650 | [78,306] | [30,670] | 116,940 | 201,247 | 336,271 |
| Statement of Financial Position Information | | | | | | | |
| Assets | | | | | | | |
| Cash in hand and cash at bank | 418,885 | 401,301 | 380,830 | 351,903 | 180,104 | 156,130 | 97,260 |
| Deposits with banks | 1,509,597 | 118,933 | 440,093 | 1,674,998 | 784,480 | 140,242 | - |
| Reverse repurchase agreement | 1,302,748 | 265,687 | 785,965 | 465,211 | 140,768 | 116,532 | 450,000 |
| Financial assets designated at FVPL | 231,264 | 323,655 | 541,970 | 882,176 | 262,817 | 311,676 | 280,815 |
| Bills receivable | 494,096 | 739,403 | 595,888 | 646,124 | 627,283 | 525,741 | 527,022 |
| Loans & advances to customers | 12,598,133 | 11,320,845 | 8,406,632 | 7,954,469 | 2,342,414 | 1,698,280 | 1,452,314 |
| Lease and hire purchase rental receivable | 15,661,432 | 14,991,751 | 14,223,259 | 12,168,389 | 6,935,706 | 7,062,055 | 5,534,145 |
| Financial investments - available for sale | 1,815,181 | 2,735,645 | 1,754,207 | 1,178,814 | 667,855 | 695,868 | 424,127 |
| Financial investments - Held to maturity | 479,362 | 57,766 | 56,507 | 653,338 | - | - | - |
| Investment in associate & subsidiary companies | 102,201 | 158,390 | 391,281 | 597,180 | 1,008,106 | 678,823 | 629,484 |
| Property & equipment, intangible assets and investment properties | 671,726 | 470,738 | 403,918 | 373,195 | 95,132 | 107,675 | 54,201 |
| Other assets | 360,582 | 342,640 | 294,000 | 368,127 | 224,135 | 398,289 | 378,374 |
| Total assets | 35,645,207 | 31,926,754 | 28,274,547 | 27,313,923 | 13,268,800 | 11,891,311 | 9,827,742 |

Decade at a Glance

Based on Financial Statements Prepared Under SLFRS

| For the year ended 31 December | 2017 | 2016 | 2015 | Company 2014 | 2013 | 2012 | 2011 |
|---|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|------------------|
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| | | Restated | | Restated | | | |
| Operating Results | | | | | | | |
| Income | 6,402,825 | 4,888,155 | 4,216,991 | 4,734,641 | 2,355,366 | 1,869,714 | 1,393,526 |
| Interest expenses | 3,708,808 | 2,709,604 | 2,133,325 | 2,579,431 | 1,371,937 | 1,035,739 | 541,370 |
| Net interest income | 2,448,478 | 2,028,170 | 1,939,834 | 1,805,198 | 893,899 | 779,559 | 782,407 |
| Operating expenses & provisions | 2,465,367 | 1,945,654 | 2,119,094 | 2,101,923 | 807,547 | 590,572 | 483,141 |
| Share of associate company | - | - | - | - | - | - | 60,248 |
| Profit before income tax | 228,650 | 232,897 | (35,428) | 53,287 | 175,882 | 243,403 | 429,263 |
| Income tax on profit | 127,799 | 154,247 | 42,878 | 83,957 | 58,942 | 42,156 | 92,992 |
| Profit after income tax | 100,851 | 78,650 | (78,306) | (30,670) | 116,940 | 201,247 | 336,271 |
| Non controlling interests | - | - | - | - | - | - | - |
| Net profit attributable to equity holders of the Parent | 100,851 | 78,650 | (78,306) | (30,670) | 116,940 | 201,247 | 336,271 |
| Statement of Financial Position Information | | | | | | | |
| Assets | | | | | | | |
| Cash in hand and cash at bank | 418,885 | 401,301 | 380,830 | 351,903 | 180,104 | 156,130 | 97,260 |
| Deposits with banks | 1,509,597 | 118,933 | 440,093 | 1,674,998 | 784,480 | 140,242 | - |
| Reverse Repurchase Agreement | 1,302,748 | 265,687 | 785,965 | 465,211 | 140,768 | 116,532 | 450,000 |
| Financial assets designated at FVPL | 231,264 | 323,655 | 541,970 | 882,176 | 262,817 | 311,676 | 280,815 |
| Bills receivable | 494,096 | 739,403 | 595,888 | 646,124 | 627,283 | 525,741 | 527,022 |
| Loans & advances to customers | 12,598,133 | 11,320,845 | 8,406,632 | 7,954,469 | 2,342,414 | 1,698,280 | 1,452,314 |
| Lease and hire purchase rental receivable | 15,661,432 | 14,991,751 | 14,223,259 | 12,168,389 | 6,935,706 | 7,062,055 | 5,534,145 |
| Financial investments - available for sale | 1,815,181 | 2,735,645 | 1,754,207 | 1,178,814 | 667,855 | 695,868 | 424,127 |
| Financial investments - Held to maturity | 479,362 | 57,766 | 56,507 | 653,338 | - | - | - |
| Investment in associate & subsidiary companies | 102,201 | 158,390 | 391,281 | 597,180 | 1,008,106 | 678,823 | 629,484 |
| Property & equipment, intangible assets and investment properties | 671,726 | 470,738 | 403,918 | 373,195 | 95,132 | 107,675 | 54,201 |
| Other assets | 360,582 | 342,640 | 294,000 | 368,127 | 224,135 | 398,289 | 378,374 |
| Total assets | 35,645,207 | 31,926,754 | 28,274,547 | 27,313,923 | 13,268,800 | 11,891,311 | 9,827,742 |
| Liabilities | | | | | | | |
| Due to banks | 123,849 | 201,635 | 258,062 | 200,002 | 99,118 | 138,239 | 183,718 |
| Cash collateral on securities lent and repurchase agreements | 437,672 | 401,820 | 416,472 | 442,170 | - | 419,462 | 930,597 |
| Due to customers | 21,918,869 | 18,518,419 | 15,846,306 | 11,092,643 | - | - | - |
| Debt issued and borrowed funds | 8,818,862 | 8,722,787 | 7,883,323 | 11,141,793 | 9,623,147 | 7,946,502 | 5,356,872 |
| Other liabilities & deferred taxation | 1,112,135 | 975,578 | 862,325 | 1,285,893 | 765,659 | 693,449 | 594,280 |
| | 32,411,387 | 28,820,239 | 25,266,488 | 24,162,500 | 10,487,924 | 9,197,652 | 7,065,467 |
| Non controlling interests | - | - | - | - | - | - | - |
| Net assets | 3,233,820 | 3,106,515 | 3,008,059 | 3,151,422 | 2,780,876 | 2,693,659 | 2,762,275 |
| Capital Employed | | | | | | | |
| Stated capital | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 | 1,607,000 | 1,607,000 | 1,607,000 |
| Retained earnings & reserves | 1,109,363 | 982,058 | 883,602 | 1,026,965 | 1,173,876 | 1,086,659 | 1,155,275 |
| | 3,233,820 | 3,106,515 | 3,008,059 | 3,151,422 | 2,780,876 | 2,693,659 | 2,762,275 |

Ratios and Related Information

| For the year ended 31 December | 2017 | 2016 Restated | 2015 | Company 2014 Restated | 2013 | 2012 | 2011 |
|--------------------------------------|-------|------------------|---------|-----------------------------|-------|--------|--------|
| Operating Ratios | | | | | | | |
| Return on Net Assets - % | 3.18 | 2.57 | [2.54] | [0.97] | 4.21 | 7.47 | 12.17 |
| Net Profit - % | 1.58 | 1.61 | [1.86] | [0.65] | 4.96 | 10.76 | 24.13 |
| Return on Assets - % | 0.30 | 0.26 | [0.28] | [0.11] | 0.88 | 1.69 | 3.42 |
| Net Interest Margin - % | 7.64 | 7.18 | 7.61 | 9.96 | 8.22 | 8.37 | 11.14 |
| Cost to Income Ratio - % | 73.10 | 71.89 | 66.89 | 62.05 | 65.71 | 55.03 | 34.19 |
| Income Growth - % | 30.99 | 15.92 | [10.93] | 86.46 | 25.97 | 34.17 | [8.50] |
| Assets Growth - % | 11.65 | 12.92 | 3.52 | 75.91 | 11.58 | 21.00 | 37.62 |
| Net Assets Growth - % | 4.10 | 3.27 | [4.55] | 4.95 | 3.24 | [2.48] | 5.09 |
| Gearing Ratios | | | | | | | |
| Debt to Equity - Times | 9.68 | 8.96 | 8.11 | 3.88 | 3.50 | 3.16 | 2.34 |
| Interest Cover - Times | 1.06 | 1.09 | 0.98 | 1.02 | 1.13 | 1.24 | 1.79 |
| Liquidity Ratios | | | | | | | |
| Quick Ratio - Times | 0.77 | 0.66 | 0.76 | 0.88 | 0.69 | 0.75 | 1.15 |
| Investors Ratios | | | | | | | |
| Market value of a voting share - Rs. | 13.5 | 13.6 | 15.00 | 17.50 | 13.60 | 19.90 | 39.60 |
| Basic Earnings Per Share - Rs. | 0.6 | 0.5 | [0.47] | [0.18] | 0.87 | 1.49 | 2.49 |
| Net Assets Value Per Share - Rs. | 19.5 | 18.73 | 18.13 | 19.00 | 20.60 | 19.95 | 20.46 |
| Price Earnings Ratio - Times | 22.20 | 28.68 | [31.77] | [94.65] | 15.70 | 13.35 | 15.90 |
| Earning Yield - % | 4.50 | 3.49 | [3.15] | [1.06] | 6.37 | 7.49 | 6.29 |

Decade at a Glance

Based on Financial Statements Prepared Under SLFRS

| For the year ended 31 December | Group | | | | | | |
|---|-------------------|-----------------------------|-------------------|-----------------------------|-------------------|-------------------|-------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2015 Rs.'000 | 2014 Rs.'000 Restated | 2013 Rs.'000 | 2012 Rs.'000 | 2011 Rs.'000 |
| Operating Results | | | | | | | |
| Income | 7,079,110 | 6,099,998 | 5,429,495 | 6,023,040 | 5,227,315 | 3,955,749 | 3,009,426 |
| Interest expenses | 3,708,625 | 2,710,557 | 2,134,351 | 2,583,660 | 2,364,151 | 1,989,101 | 1,234,716 |
| Net interest income | 2,547,987 | 2,142,450 | 2,029,708 | 1,901,069 | 1,432,656 | 1,475,261 | 1,400,392 |
| Operating expenses & provisions | 3,132,083 | 3,144,178 | 3,246,223 | 3,441,106 | 2,943,460 | 1,698,689 | 1,344,174 |
| Share of associate company | 1,059 | (5,437) | 7,080 | 17,208 | (606) | (17,486) | 60,248 |
| Profit before income tax | 239,461 | 239,826 | 56,001 | 15,483 | (80,902) | 250,473 | 490,784 |
| Income tax on profit | 136,111 | 165,658 | 52,718 | 86,016 | 78,851 | 70,256 | 125,318 |
| Profit after income tax | 103,349 | 74,168 | 3,283 | (70,532) | (159,753) | 180,217 | 365,466 |
| Non controlling interests | (8,508) | (36,711) | (18,869) | (9,386) | (57,632) | 36,724 | 30,703 |
| Net profit attributable to equity holders of the Parent | 111,858 | 110,879 | 22,152 | (61,146) | (102,121) | 143,493 | 334,763 |
| Statement of Financial Position Information | | | | | | | |
| Assets | | | | | | | |
| Cash in hand and cash at bank | 466,139 | 441,357 | 432,947 | 406,132 | 275,688 | 317,758 | 247,625 |
| Deposits with banks | 1,597,785 | 262,319 | 571,672 | 1,796,986 | 1,186,017 | 485,954 | 274,243 |
| Reverse repurchase agreement | 1,651,927 | 730,773 | 1,609,702 | 1,313,486 | 469,958 | 590,525 | 552,218 |
| Financial assets designated at FVPL | 238,252 | 331,586 | 552,741 | 896,629 | 285,545 | 373,391 | 387,609 |
| Bills receivable | 494,096 | 739,403 | 595,888 | 646,124 | 627,283 | 525,743 | 527,024 |
| Loans & advances to customers | 12,592,956 | 11,392,491 | 8,505,054 | 8,097,427 | 3,640,429 | 4,458,095 | 4,382,575 |
| Lease and hire purchase rental receivable | 15,661,432 | 14,991,751 | 14,223,259 | 12,168,389 | 7,959,842 | 11,971,076 | 9,316,466 |
| Financial investments-available-for-sale | 2,191,842 | 3,126,815 | 1,994,857 | 1,221,417 | 1,427,400 | 1,161,481 | 1,238,225 |
| Financial investments-held-to-maturity | 479,362 | 57,766 | 56,507 | 653,338 | 100,957 | 507,737 | 308,216 |
| Investment in associate & subsidiary companies | 92,453 | 91,325 | 96,484 | 94,454 | 438,234 | 106,228 | 132,774 |
| Property & equipment, intangible assets and investment properties | 715,692 | 533,816 | 486,103 | 491,792 | 393,956 | 419,012 | 301,276 |
| Other assets | 735,030 | 935,061 | 774,877 | 805,625 | 753,263 | 1,245,877 | 1,299,234 |
| Total assets | 36,916,966 | 33,634,463 | 29,900,092 | 28,591,799 | 17,558,572 | 22,162,877 | 18,967,485 |

| For the year ended 31 December | Group | | | | | | |
|--|------------------------|-----------------------------|-------------------|-----------------------------|-------------------|-------------------|-------------------|
| | 2017 Rs.'000 | 2016 Rs.'000 Restated | 2015 Rs.'000 | 2014 Rs.'000 Restated | 2013 Rs.'000 | 2012 Rs.'000 | 2011 Rs.'000 |
| Liabilities | | | | | | | |
| Due to banks | 129,877 | 224,997 | 273,968 | 210,011 | 152,338 | 272,994 | 520,638 |
| Cash collateral on securities lent and repurchase agreements | 437,672 | 401,820 | 416,472 | 442,170 | - | 435,558 | 930,597 |
| Due to customers | 21,910,383 | 18,518,419 | 15,846,306 | 11,092,643 | 2,824,918 | 7,546,297 | 6,983,892 |
| Debt issued and borrowed funds | 8,818,862 | 8,722,787 | 7,883,323 | 11,141,793 | 9,625,317 | 8,555,028 | 5,622,322 |
| Other liabilities & deferred taxation | 2,361,016 | 2,626,857 | 2,425,245 | 2,580,518 | 2,048,486 | 1,950,552 | 1,473,646 |
| | 33,657,810 | 30,494,880 | 26,845,314 | 25,467,138 | 14,651,059 | 18,760,429 | 15,531,095 |
| Non controlling interests | 7,146 | 14,343 | 52,673 | 72,715 | 139,805 | 504,924 | 461,072 |
| Net assets | 3,278,881 | 3,139,583 | 3,002,104 | 3,051,944 | 2,767,708 | 2,897,524 | 2,975,318 |
| Capital Employed | | | | | | | |
| Stated capital | 2,124,457 | 2,124,457 | 2,124,457 | 2,124,457 | 1,607,000 | 1,607,000 | 1,607,000 |
| Retained earnings & reserves | 1,147,278 | 1,000,783 | 877,647 | 927,492 | 1,160,707 | 1,290,524 | 1,368,318 |
| | 3,271,735 | 3,125,240 | 3,002,104 | 3,051,949 | 2,767,707 | 2,897,524 | 2,975,318 |

Decade at a Glance

Ratios and Related Information

| For the year ended 31 December | 2017 | 2016 Restated | 2015 | Group | | 2012 | 2011 |
|--------------------------------------|-------|------------------|--------|------------------|---------|--------|-------|
| | | | | 2014 Restated | 2013 | | |
| Operating Ratios | | | | | | | |
| Return on Net Assets - % | 3.24 | 2.42 | 0.11 | (2.31) | (3.69) | 4.95 | 11.25 |
| Net Profit - % | 1.46 | 1.22 | 0.06 | (1.17) | (3.06) | 4.56 | 12.14 |
| Return on Assets - % | 0.29 | 0.23 | 0.11 | (0.25) | (0.91) | 0.81 | 1.93 |
| Net Interest Margin - % | 7.72 | 7.28 | 7.59 | 9.20 | 8.16 | 8.13 | 16.87 |
| Cost to Income Ratio - % | 77.48 | 84.23 | 76.78 | 70.71 | 96.98 | 77.62 | 59.82 |
| Income Growth - % | 16.05 | 12.35 | (9.85) | 41.91 | 32.14 | 31.45 | 15.94 |
| Assets Growth - % | 9.76 | 12.49 | 4.58 | 48.38 | (20.77) | 16.85 | 31.95 |
| Net Assets Growth - % | 3.81 | 4.58 | 0.09 | 8.01 | (4.48) | (2.61) | 4.01 |
| Gearing Ratios | | | | | | | |
| Debt to Equity - Times | 9.62 | 8.92 | 7.99 | 3.86 | 3.53 | 3.20 | 2.38 |
| Interest Cover - Times | 1.06 | 1.09 | 1.03 | 1.01 | 0.97 | 1.13 | 1.40 |
| Liquidity Ratios | | | | | | | |
| Quick Ratio - Times | 0.80 | 0.69 | 0.82 | 0.81 | 0.69 | 0.63 | 0.85 |
| Investors Ratios | | | | | | | |
| Market Value of a voting share - Rs. | 13.5 | 13.6 | 15.00 | 17.50 | 13.60 | 19.90 | 39.60 |
| Basic Earnings Per Share - Rs. | 0.67 | 0.67 | 0.02 | (0.43) | (0.76) | 1.06 | 2.48 |
| Net Assets Value Per Share - Rs. | 19.7 | 18.8 | 18.10 | 18.40 | 20.50 | 21.46 | 22.04 |
| Price Earnings Ratio - Times | 0.05 | 0.05 | 0.00 | (41.16) | (17.98) | 18.72 | 15.97 |
| Earning Yield - % | 5.00 | 4.92 | 0.00 | (0.02) | (5.56) | 5.34 | 6.26 |

Independent Assurance Report



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Sri Lanka

INDEPENDENT ASSURANCE REPORT TO THE STAKEHOLDERS OF MERCHANT BANK OF SRI LANKA & FINANCE PLC ON THE SUSTAINABILITY REPORT – 2017

INTRODUCTION AND SCOPE OF THE ENGAGEMENT

The management of Merchant Bank of Sri Lanka & Finance PLC [“the company”] engaged us to provide an independent assurance on the following elements of the Sustainability Report 2017 [“the Report”].

- Reasonable assurance on the information on financial performance as specified on page 27 of the Report.
- Limited assurance on key performance indicators and other information presented in the Report prepared in accordance with Global Reporting Initiative Standards [GRI Standards].

RESPONSIBILITY OF THE MANAGEMENT ON THE REPORT

The Management of the Company is responsible for the preparation and presentation of the Report in accordance with the Company’s sustainability practices and policies which are derived from GRI Standards. These responsibilities include among other things, identification of stakeholders and material issues, determining the sustainable performance criteria for reporting and establishing appropriate processes and internal control systems to measure and report the sustainability performance criteria.

OUR RESPONSIBILITY

Our responsibility is to perform a reasonable and limited assurance engagement and express conclusions based on the work performed in accordance with Sri Lanka Standard on Assurance Engagements [SLSAE 3000]: ‘Assurance Engagements other than Audits or Reviews of Historical Financial Information’, issued by the Institute of Chartered Accountants of Sri Lanka [‘CASL’].

Reasonable assurance is a high level of assurance. However, reasonable assurance is not an absolute level of assurance because there are inherent limitations of assurance engagement.

A limited assurance engagement is substantially less in scope than a reasonable assurance engagement and consequently does not enable to obtain assurance that we would become aware of all significant matters that might be identified in a reasonable assurance engagement.

This Report is made solely to the Company in accordance with our engagement letter dated 27 April 2018. We disclaim any assumption of responsibility for any reliance on this Report to any person other than the Company or for any purpose other than that for which it was prepared. In conducting our engagement, we have complied with the independence requirements of the Code of Ethics for professional Accountants issued by the CA Sri Lanka.

ASSURANCE PROCEDURES CARRIED OUT

Financial Information

We reconciled the information on financial performance as reported on page 27 of the Report with the audited financial statements of the Company for the years ended 31st December, 2016 and 2017.

Key Performance Indicator

We reviewed the reliability of the data/information on Key Performance Indicator for the year ended 31st December, 2017 based on reviews of:

- the system used to generate, aggregate and report these information;
- the information reported by the relevant business units to corporate level;
- the information validation processes at corporate and business level;
- the information trends in discussions with management and
- the calculation performed by the company on a sample basis

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Partners : Sujeewa Rajapakse FCA, FCMA, MBA. H.Sasanka Rathnaweera FCA, ACMA. Ashane J.W. Jayasekara FCA, FCMA (UK), MBA. Hasanthi D.Amarakoon ACA, ACMA. R. Vasanthakumar Bsc (Acc), ACA

Independent Assurance Report

through recalculation.

Other Information

We planned and performed following assurance procedures in other information presented in the Report:

- Inquiring relevant Company's personnel to understand the process for collection, analysis, aggregation and presentation of information in the Report.
- Reviewing the system used to generate, aggregate and report the information in the Report.
- Interviewing the senior management and relevant staff at corporate level and selected business unit level and obtained the evidence concerning sustainability strategy and policies for material issues and implementation of those across operation of the company.
- Reviewing and validating the information contained in the Report.
- Reading the information presented in the Report to determine whether that information is in line with our overall knowledge of, and experience with, sustainability performance of the Company.
- Comparison of the content of the report against the criteria of GRI Standards.

CONCLUSION

Based on the procedures performed, as described above, we conclude that:

- The information on financial performance as specified on page 27 of the Report is properly derived from the audited financial statements of the company for the years ended 31st December, 2016 and 2017.
- Nothing has come to our attention that causes us to believe that key performance indicators and other information presented in the Report are not presented, in all material respects, in accordance with the Company's sustainability practices and policies which are derived from GRI Standards..

CHARTERED ACCOUNTANTS

BDO Partners

Colombo

27 April 2018

GRI Checklist

| GRI Standard | Disclosure | Page number |
|---|---|---------------|
| GRI 101: Foundation 2016 | (does not include any disclosures) | |
| General Disclosures | | |
| GRI 102: General Disclosures 2016 | 102-1 Name of Organisation | 4 |
| | 102-2 Activities, brands, products and services | 11 |
| | 102-3 Location of headquarters | 260 |
| | 102-4 Location of operations | 37 |
| | 102-5 Ownership and legal form | 260 |
| | 102-6 Markets served | 37,46,252-259 |
| | 102-7 Scale of the organisation | 4,10 |
| | 102-8 Information on employees and other workers | 38 |
| | 102-9 Supply chain | 47 |
| | 102-10 Significant changes to the organisation and supply chain | 47 |
| | 102-11 Precautionary principle | 49 |
| | 102-12 External initiatives | 47 |
| | 102-13 Membership of associations | 46 |
| | 102-14 Statement from senior decision maker | 8 |
| | 102-16 Values, principles, norms and standards of behavior | 46,1 |
| | 102-18 Governance Structure | 63 |
| | 102-40 List of stakeholder groups | 16 |
| | 102-41 Collective bargaining agreements | 40 |
| | 102-42 Identifying and selecting stakeholders | 16 |
| | 102-43 Approach to stakeholder engagement | 16 |
| | 102-45 Entities included in the consolidated financial statements | 4 |
| | 102-44 Key topics and concerns raised | 16 |
| | 102-46 Defining report content and topic boundary | 5,19 |
| | 102-47 Material topics | 19 |
| | 102-48 Restatement of information | 5 |
| | 102-49 Changes in reporting | 19 |
| 102-50 Reporting period | 4 | |
| 102-51 Date of most recent report | 4 | |
| 102-52 Reporting cycle | 4 | |
| 102-53 Contact point for questions regarding Report | 4 | |
| 102-54 Claims of reporting in accordance with GRI Standards | 4 | |
| 102-55 GRI context index | 241-244 | |
| 102-56 External assurance | 4,239 | |

GRI Checklist

| GRI Standard | Disclosure | Page number |
|-------------------------------------|---|-------------------------|
| Material topics | | |
| Economic Performance | | |
| GRI 103: Management Approach | 103-1 Explanation of material topics and its boundaries | 25 |
| | 103-2 The Management Approach and its components | 25 |
| | 103-3 Evaluation of the Management Approach | 25 |
| GRI 201: Economic Performance 2016 | 201-1- Direct economic value generated and distributed | 14 |
| | 201-3 Defined benefit plan obligations and other retirement plans | 41 |
| Market Presence | | |
| GRI 202: Market Presence | 202-2 Proportion of senior management hired from the local community | 39 |
| GRI 203: Indirect Economic Impacts | | Information unavailable |
| Procurement Practices | | |
| GRI 204: Procurement Practices | 204-1 Proportion of spending on local suppliers | 47 |
| Anti-Corruption | | |
| GRI 205: Anti-Corruption | 205-2 Communication and training about anti-corruption policies and procedures | 40 |
| Anti-Competitive Behavior | | |
| GRI 206: Anti-Competitive Behaviour | 206-1 Legal actions for anti-competitive behavior, anti-trust, and monopoly practices | 40 |
| Materials | | |
| GRI 103: Management Approach | 103-1 Explanation of material topics and its boundaries | 49 |
| | 103-2 The Management Approach and its components | 49 |
| | 103-3 Evaluation of the Management Approach | 49 |
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Basis of Ratio

| | | |
|--|--|------|
| Return on Equity (ROE) | Profit / Loss Attributable to Ordinary Share | *100 |
| | Average Shareholder's Equity | |
| Return on Capital Employed (ROCE) | Profit before Interest & Tax | *100 |
| | Borrowings+Deposits+Equity | |
| Cost to Income Ratio | Total Operating cost Without VAT on Financial Services | *100 |
| | Net Operating Income | |
| Debt to Equity (Times) | Total Borrowings | |
| | Total Shareholder's Equity | |
| Debt to Total Assets (Times) | Borrowings | |
| | Total Assets | |
| Earning Per Share (EPS - Rs:) | Profit / Loss Attributable to ordinary shareholders | |
| | Average Number of Share | |
| Price Earning (PE) Ratio (Times) | Market Price Per Share | |
| | Earning Per Share | |
| Dividend Per Share (Rs:) | Profit / Loss Attributable to Ordinary Share | |
| | Number of Ordinary Share | |
| Dividend Yield (%) | Dividend Per Ordinary Share | *100 |
| | Market Price Per Share | |
| Market Capitalization (Rs) | Market Price Per Share * Number of Shares | |
| Total Return of Share (%) | [Closing Market Price - Opening Market Price] + Dividend Per Share | *100 |
| | Openning Market Price | |

Basis of Ratio

| | | |
|---|---|------|
| Return on Assets (ROA) - % | Profit After tax | *100 |
| | Total Assets | |
| Operating Profit Margin - % | Operating Profit Before VAT on Financial Services | *100 |
| | Interest Income | |
| Interest Cover (Times) | Profit Before Interest & Tax | |
| | Interest Expenses | |
| Current Ratio | Current Assets | |
| | Current Liabilities | |
| Net Assets Value Per Share (NAPS -Rs:) | Total Share Holders Equity | |
| | Number of Share | |
| Earning Yield (EY) | Earning Per Share | *100 |
| | Market Price Per Share | |
| Dividend Cover Ratio (Times) | Profit / Loss Attributable to Ordinary Shareholders | |
| | Total Dividend Paid to Shareholders | |
| Dividend Pay Out (%) | Total Dividend Paid to Shareholders | |
| | Profit / Loss Attributable to Ordinary Shareholders | |
| Price to Book Value (PBV - Times) | Market Price Per Share | |
| | Net Assets Per Share | |
| Net Interest Margin (NIM - %) | Net Interest Income | *100 |
| | Average Interest Earnings Assets | |

GLOSSARY OF FINANCIAL STATEMENTS

A

Accounting Policies

The specific principles, bases, conventions, rules and practices adopted by an entity in preparing and presenting Financial Statements.

Accrual Basis

Recognising the effects of transactions and other events when they occur without waiting for receipt or payment of cash or its equivalent.

Amortisation

The systematic allocation of the depreciable amount of an asset over its useful life.

Associate company

An entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.

Available-for-Sale Financial assets

All non-derivative financial assets that does not fall into any of the three categories, namely, held to maturity, Fair Value through Profit or Loss and Loans & Receivable. It is a residual category - does not mean that the entity stands ready to sell these all the time.

C

Capital Adequacy Ratio

The ratio between capital and risk-weighted assets as defined in the framework developed by the Bank for International Settlements (BIS) and as modified by the Central Bank of Sri Lanka to suit local requirements.

Cash equivalents

Short-term highly liquid investments which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Collective Impairment Provisions

Impairment is measured on a collective basis for homogeneous groups of loans that are not considered individually significant.

Commercial Paper

An unsecured short term debt instrument issued by a corporation, typically for the financing of accounts receivable, inventories and meet short-term liabilities. The debt is usually issued at a discount, reflecting prevailing market interest rates.

Commitments

Credit facilities approved but not yet utilized by the clients as at the reporting date.

Compounded Annual Growth Rate [CAGR]

The rate at which it would have grown if it grew at an even rate compounded annually.

Consolidated Financial Statements

Financial statements of a holding company and its subsidiaries based on their combined assets, liabilities and operating results.

Contingencies

A condition or situation existing on the statement of financial position where the outcome will be confirmed only by occurrence or non-occurrence of one or more future events.

Cost / Income Ratio

A ratio expressing Company's cost effectiveness which sets operating expenses including Financial Value Added Tax and excluding Loan Loss Provision in relation to operating income.

Cost Method

This is a method of accounting for an investment whereby the investment is initially recognised at cost. The investor recognises income from the investment only to the extent that the investor receives distributions from accumulated profits of the investee arising after the date of acquisition. Distributions received in excess of such profits are regarded as a recovery of investment and are recognised as a reduction of the cost of the investment.

Corporate Governance

The process by which corporate entities are governed. It is concerned with the way in which power is exercised over the management and direction of entity, the supervision of executive actions and accountability to owners and others.

Credit Risk

Credit risk or default risk is the potential that a borrower or counterparty failing to meet its obligations in accordance with agreed terms and conditions.

Credit Ratings

An evaluation of a corporate's ability to repay its obligations or the likelihood of not defaulting, carried out by an independent rating agency.

GLOSSARY OF FINANCIAL STATEMENTS

D

Deferred Taxation

Sum set aside for income tax in the Financial Statements that may become payable/receivable in a financial year other than the current financial year.

Depreciation

The systematic allocation of the depreciable amount of an asset over its useful life.

Dividend Cover

Profit attributable to shareholders divided by gross dividends. This ratio measures the number of times dividend is covered by current year's attributable profits.

Dividend Yield

Dividend per share as a percentage of its market value.

E

Earnings per Ordinary share (EPS)

Profit attributable to ordinary shareholders divided by the number of ordinary shares in issue.

Economic Value Added (EVA)

A measure of productivity that takes into consideration cost of total invested equity.

Effective Interest Rate (EIR)

The rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

Effective Tax Rate

Provision for taxation excluding deferred tax expressed as a percentage of the profit before taxation.

Equity Method

This is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition changes in the investor's share of net assets of the investee. The profit or loss of the investor includes the investor's share of the profit or loss of the investee.

F

Fair Value

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

Fair Value Through Profit or Loss

A financial asset/liability: Acquired/incurred principally for the purpose of selling or repurchasing it in the near term, part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking, or a derivative (except for a derivative that is a financial guarantee contract)

Financial Asset

Any asset that is cash, an equity instrument of another entity or a contractual right to receive cash or another financial asset from another entity.

Financial Liability

A contractual obligation to deliver cash or another financial asset to another entity.

Finance Lease

A contract whereby a lessor conveys to the lessee the right to use an asset for rent over an agreed period of time which is sufficient to amortise the capital outlay of the lessor. The lessor retains ownership of the asset but transfers substantially all the risks and rewards of ownership to the lessee.

Financial Instrument

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

G

Gearing

Long term borrowings divided by the total funds available for shareholders.

Group

A group is a parent and all its subsidiaries.

Guarantees

Three party agreement involving a promise by one party (the guarantor) to fulfil the obligations of a person owing a debt if that person fails to perform.

H

Held-to-Maturity (HTM) Investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and a fixed maturity that an entity has the positive intention and ability to hold till maturity.

I

Impairment

This occurs when recoverable amount of an asset is less than its carrying amount.

Impaired Loans

Loans where identified impairment provisions have been raised and also include loans which are collateralised or where indebtedness has already been written down to the expected realisable value. The impaired loan category may include loans, which, while impaired, are still performing.

Individually Assessed Impairment

Exposure to loss is assessed on all individually significant accounts and all other accounts that do not qualify for collective assessment.

Impairment Allowances

Impairment allowances are a provision held as a result of the raising of a charge against profit for the incurred loss.

Intangible Asset

An intangible asset is an identifiable non-monetary asset without physical substance.

Interest cover

A ratio showing the number of times interest charges are covered by earnings before interest and tax.

Interest Margin

Net interest income expressed as a percentage of average interest earnings assets.

Interest rate risk

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of the changes in market interest rates.

Interest Spread

Represents the difference between the average interest rate earned on interest earnings assets and the average interest rate paid on interest-bearing liabilities.

Investment properties

Investment property is property (land or a building – or part of a building – or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both rather than for use or sale.

K

Key Management Personnel (KMP)

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any Director (whether Executive or otherwise) of that entity.

L

Liquid Assets

Assets that are held in cash or in a form that can be converted to cash readily, such as deposits with Banks, bills of exchange and Treasury Bills and Bonds.

Loan to Value Ratio (LTV)

LTV ratio is a computation that expresses the amount of a first disbursement as a percentage of the total appraised value of assets kept as security.

Liquidity Risk

The risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

Loans and Receivables

Conventional loan assets that are unquoted (originated or acquired).

M

Market Capitalisation

Number of ordinary shares in issue multiplied by the market value of a share as at the year end.

GLOSSARY OF FINANCIAL STATEMENTS

Market Risk

This refers to the possibility of loss arising from changes in the value of a financial instrument as a result of changes in market variables such as interest rates, exchange rates, credit spreads and other asset prices.

Materiality

The relative significance of a transaction or an event, the omission or misstatement of which could influence the economic decisions of users of Financial Statements.

N

Net Assets Value per Ordinary Share

Shareholders' funds excluding preference shares, if any, divided by the number of ordinary shares in issue.

Net Interest Income (NII)

The difference between income earned from interest bearing assets and cost incurred on financial instrument / facilities used for funding the interest bearing assets.

Non-Controlling Interest

Equity in a subsidiary not attributable, directly or indirectly, to a parent.

Non-performing ratio

Total non-performing leases, hire purchase loans and other advances divided by total advances portfolio.

O

Off-Balance Sheet Transactions

Transactions that are not recognised as assets or liabilities in the Balance Sheet, but which give rise to contingencies and commitments.

Operational Risk

This refers to the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

P

Parent

A Parent is an entity which has one or more subsidiaries.

Price Earnings Ratio (P/E Ratio)

Market price of an ordinary share divided by earnings per share.

Prudence

Inclusion of a degree of caution in the exercise of judgment needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.

R

Related Parties

Parties where one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions, directly or indirectly.

Return on Assets (ROA)

Profit after tax expressed as a percentage of the average assets.

Risk weighted assets

On statement of financial position assets and the credit equivalent of off-balance sheet assets multiplied by the relevant risk weighting factors.

Repurchase Agreement

Contract to sell and subsequently repurchase securities at a specified date and price.

Return on Equity (ROE)

Net profit for the year, less dividends on preference shares, if any, expressed as a percentage of average ordinary shareholders' equity.

Reverse Repurchase Agreement

Transaction involving the purchase of securities by a bank or a dealer and resale back to the seller at a future date at a specified price.

Rights Issue

Issue of shares to the existing shareholders at an agreed price, generally lower than market price.

S

Segment analysis

Analysis of financial information by segments of an entity specifically the different business in which it operates.

Shareholders' Funds

Total of stated capital and reserves.

Specific Impairment Provisions

Impairment is measured individually for loans that are individually significant to the Company.

Subsidiary Company

A subsidiary is an enterprise that is controlled by another enterprise which is known as the parent.

Substance over Form

The consideration that the accounting treatment and the presentation in Financial Statements of transactions and events should be governed by their substance and financial reality and not merely by legal form.

T

Transaction costs

Incremental costs that is directly attributable to the acquisition, issue or disposal of a financial asset or financial liability

V

Value Added

Value of wealth created by providing financial and other-related services less the cost of providing such services.

Y

Yield to Maturity

Discount rate at which the present value of future cash flows would equal the security's current price.

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| Mr. Ratnasiri Mayakaduwa Acting Assistant General Manager | 091-4650200 | 077-3047787 | No.39B,B2, Lower Dickson Rd, Walawwatta, Galle. | 091-4650205 | ratnasirim@mbslbank.com |
| GALLE BRANCH | | | | | |
| Mr. Gayan Nilanga Manager | 091-4 711711 091-4 711700 091-2234751 | 077-3219583 | No.35,37 New Street, Galle. | 091-2234750 | gayann@mbslbank.com |
| RATNAPURA BRANCH | | | | | |
| Mr. Chinthaka Athukorala Branch Manager | 045-4928089 045-4928093 | 077-3241089 | No.231, Main Street, Rathnapura. | 045-2232524 | chinthakaa@mbslbank.com |
| AMBALANGODA BRANCH | | | | | |
| Mr. W W A Dharmendra Branch Manager | 091-4943759 091-4943765 | 077-3240887 | No.45, Station Road, Ambalangoda | 091-2256675 | dharmendraa@mbslbank.com |

Contact Information

| REGIONAL OFFICES | Telephone | Mobile No | Address | Fax | Email |
|---|---|-------------|--|-------------|-------------------------|
| AMBALANTHOTA BRANCH | | | | | |
| Mr. Kishan Keerthi Branch Manager | 047-4711700 | 077-3240572 | No:133, Main street, Ambalanthota | 047-2225610 | keerthid@mbslbank.com |
| DENIYAYA BRANCH | | | | | |
| Mr. Manjula Prasad Krasinghe Arachchige Manager | 041-4935173 041-4935174 | 077-9286365 | 1/153 Hospitle road, Deniyaya | 041-2273731 | manjulak@mbslbank.com |
| EMBILIPITIYA BRANCH | | | | | |
| Mr. Priyajith Subasinghe Branch Manager | 047-4931992 047-4931993 | 077-3240827 | 79/A, New Town Road, Embilipitiya | 047-2261735 | priyajiths@mbslbank.com |
| MATARA BRANCH | | | | | |
| Mr. Shyaman Karunanayaka Manager | 041 4 650 400 041 4 650 420 | 077-5506573 | No:344/F, Anagarika Dharmapala Mawatha, Nupe, Matara. | 041-2233886 | shyamank@mbslbank.com |
| MATHUGAMA BRANCH | | | | | |
| Mr. Emil Cooray Branch Manager | 034-4947811 034-4947812 | 077-3240846 | No.92/4, Agalawatta Road, Mathugama | 034-2249992 | emilc@mbslbank.com |
| TISSAMAHARAMA BRANCH | | | | | |
| Mr. Pathum De Silva Branch Manager | 047-2238716 | 077-4955211 | No.117, Palliyawatta Junction, Helambagaswala Road, Tissamaharama. | 047-2238717 | pathums@mbslbank.com |
| KALUTHARA BRANCH | | | | | |
| Mr. Pathum Dassanayake Branch Manager | 034-2224245 | 077-6720861 | 426, Galle Road, Kalutara South. | 034-2229482 | pathumd@mbslbank.com |
| REGION 04 | | | | | |
| Mr. Keerthi Ramanayake Regional Manager | 081-2224820 | 077-3219578 | 284, Katugasthota Road, Kandy. | 081-2202215 | keerthir@mbslbank.com |
| KANDY BRANCH | | | | | |
| Mr. Chaminda Amarasinghe Manager | 081-4951786 081-2224818 081-2224819 | 077-3047775 | 284, Katugasthota Road, Kandy. | 081-2213880 | chamindaa@mbslbank.com |
| KANDY BRANCH - CITY OFFICE | | | | | |
| Mr. Nimal Hataraliyadda Manager | 081-2237378 081-2237380 | 077-6690164 | "Ceybank House" No.88, Dalada Veediya, Kandy. | 081-2237378 | nimalh@mbslbank.com |

| REGIONAL OFFICES | Telephone | Mobile No | Address | Fax | Email |
|---|--|-------------|--|-------------|------------------------|
| AMPARA BRANCH | | | | | |
| Mr. Chaminda Kadigamuwa Acting Branch Manager | 063-4923540 063-4923541 | 077-3240817 | No.6, D S Senanayake Mw, Ampara | 063-2224260 | sanjeewac@mbslbank.com |
| BANDARAWELA BRANCH | | | | | |
| Mr. Sumith Karunaratne Branch Manager | 057-4926910 057-4926911 | 077-3240329 | No.11,Badulla Road, Thanthiriya, Bandarawela | 057-2233807 | sumiths@mbslbank.com |
| BATTICALOA BRANCH | | | | | |
| Mr. P Nivaraj Manager | 065-4926799 065-4926787 | 077-3240721 | No:28, Bar Road, Batticaloa | 065-2228575 | nivarajp@mbslbank.com |
| DAMBULLA BRANCH | | | | | |
| Mr. Sumith Premarathne Branch Manager | 066-2284205 | 077-1912084 | 1/690, Anuradhapura Road, Dambulla. | 066-2284204 | sumithp@mbslbank.com |
| HATTON BRANCH | | | | | |
| Mr. Perumal Baskar Branch Manager | 051-4924641 051-4924642 | 077-3241135 | No: 263, Dimbula Road, Hatton | 051-2224375 | baskarp@mbslbank.com |
| MONARAGALA BRANCH | | | | | |
| Mr. Ajith Priyantha Branch Manager | 055-4929361 055-4929362 | 077-3240193 | No.280, Wellawaya Road, Monaragala | 055-2276087 | ajithp@mbslbank.com |
| REGION 05 | | | | | |
| Mr. S P Niroshan Regional Manager | 031-2237355 | 0777514795 | No:329/16, Main Street, Negombo | 031-2228466 | niroshans@mbslbank.com |
| NEGOMBO BRANCH | | | | | |
| Mr. Pandula Bandara Manager | 031-2228325 031-4932230 | 077-4467507 | No. 329/16, Main Street, Negombo | 031-2228324 | pandulab@mbslbank.com |
| CHILLAW BRANCH | | | | | |
| Mr. Nuwan Prasanga Branch Manager | 032-2224414 032-2224415 032-4928790 032-4928791 | 077-3973424 | No. 6, Ebert Silva Estate, Colombo Road, Chillaw. | 032-2224033 | nuwanp@mbslbank.com |
| WENNAPPUWA BRANCH | | | | | |
| Mr. Dimuth Fernando Acting Branch Manager | 031-2245664 031-2245665 | 077-6744703 | No.177, Samagi Building, Chillaw Road, Kolinjadiya, Wennappuwa. | 031-2249979 | dimuthf@mbslbank.com |

Contact Information

| REGIONAL OFFICES | Telephone | Mobile No | Address | Fax | Email |
|--|----------------------------|-------------|--|---------------|-------------------------|
| PUTTALAM BRANCH | | | | | |
| Mr. Chaminda Pushpakumara Branch Manager | 032-4928795 032-4928796 | 077-1024291 | No.126/B, Kurunegala Road, Puttalam. | 032-2267776 | chamindam@mbslbank.com |
| KULIYAPITIYA BRANCH | | | | | |
| Mr. Malinda Pathirana Branch Manager | 037-2281731 037-4941147 | 077-6573760 | No.413/1/1, Madampe road, Kuliyapitiya. | 037-2281730 | malindap@mbslbank.com |
| JA-ELA BRANCH | | | | | |
| Mr. Pradeep Kumarage Acting-Officer-in-Charge | 011-2249292 | 077-6722479 | No.270/1, Negombo Road, Thudalla, Ja-Ela | 011-2249291 | pradeepk@mbslbank.com |
| KANDANA BRANCH | | | | | |
| Mr. Susith De Silva Branch Manager | 011 -4344073 | 072-1706482 | NO.310, Colombo Road, Kandana | 011 - 4544177 | susithd@mbslbank.com |
| WATTALA BRANCH | | | | | |
| Mr. Samith Jayasekara Branch Manager | 011-2931761 | 077-3471166 | No.500, Negambo Road, Wattala. | 011-2931762 | samithj@mbslbank.com |
| REGION 06 | | | | | |
| Mr. Saman Pathmadeera Regional Manager | 037-4711700 | 077-3219579 | No. 55, Kings Groove, Rajapihilla Road, Kurunegala | 037-2224215 | samanp@mbslbank.com |
| KURUNEGALA BRANCH | | | | | |
| Mr. Nishantha Dhahanaka Acting Manager | 037-4711710 | 077-3241323 | No. 55, Kings Groove, Rajapihilla Road, Kurunegala | 037-2224570 | nishanthad@mbslbank.com |
| ANURADHAPURA BRANCH | | | | | |
| Mr. Amila Mawathawewa Manager | 025-4580507 025-2234485 | 077-2519083 | No: 82, Maithreepala Senanayake Mawatha, Anuradhapura | 025-4580508 | amilaw@mbslbank.com |
| JAFFNA BRANCH | | | | | |
| Mr. Trevis Mohanraj Manager | 021-2220380 | 077-7562567 | No. 317, Clock Tower Road, Jaffna. | 021-2220381 | mohanrajg@mbslbank.com |
| KILINOCCHI BRANCH | | | | | |
| Mr. L Logeswaran Acting-Officer-In-Charge | 021-2280078 | 077-8744870 | No.30 Kandy Road, Karadipokku, Kilinochchi. | 021-2280079 | logesw@mbslbank.com |

| REGIONAL OFFICES | Telephone | Mobile No | Address | Fax | Email |
|--|----------------------------|-------------|---|-------------|-------------------------|
| HINGURAKGODA BRANCH | | | | | |
| Mr. Chaminda Batagoda Branch Manager | 027-4924761 027-4924762 | 077-3240274 | No.17, Air-Port Road, Damana Kumbura, Hingurakgoda | 027-2245483 | kumarab@mbslbank.com; |
| KEKIRAWA BRANCH | | | | | |
| Mr. Tharanga Buddhika Branch Manager | 025-4928951 025-4928952 | 077-3240264 | No.24, Yakalla Road, Kekirawa | 025-2264799 | tharangab@mbslbank.com |
| VAVUNIYA BRANCH | | | | | |
| Mr. R. Saravanan Senior Manager | 024-4711700 024-4711704 | 077-6519372 | No: 99, Station Road, Vavuniya | 024-2226108 | saravananr@mbslbank.com |
| TRINCOMALEE BRANCH | | | | | |
| Mr. Samson Varapragasam Branch Manager | 026-4928888 026-4595151 | 077-3650017 | No: 133, Main Street, Trincomalee | 026-2226784 | samsonv@mbslbank.com |

Corporate Information

Name of Company

Merchant Bank of Sri Lanka & Finance PLC

[Formerly known as 'Merchant Bank of Sri Lanka PLC']

Company Registration No

PQ10

Legal Form

A limited liability company incorporated on 4th March 1982 under the Companies Ordinance No. 51 of 1938 and re- registered under the Companies Act No. 07 of 2007 on 4th March 2007 and quoted on the Colombo Stock Exchange.

A Registered Finance Leasing Company under the Finance Leasing Act No. 56 of 2000.

A Registered Finance Company licensed under the Finance Business Act No. 42 of 2011.

Stock Exchange Listing

25th April 1991

Registered Office

Bank of Ceylon Merchant Tower,
No. 28, St. Michael's Road, Colombo 03
Tel. 011 4711711
Fax. 011 4711742
web. www.mbslbank.com

Tax Payer Identification No.

124011426

VAT Registration No.

124011426 7000

Central Bank registration No.

050

Financial Year End

31st December

Board of Directors:

Dr. S Lokuhewa [Chairman]
Mr. W P R P H Fonseka
Mr. K B S Bandara
Mr. S N Dayaratne [Senior Director]
Mr. N Perera
Mr. S P Arsakularatne
Mr. M P R Kumara [Alternate Director to Mr. W P R P H Fonseka]

Deputy General Manager - Legal/Company Secretary

Ms. Karnika Jayatilake
Tel: 4711766
E-mail : karnikaj@mbslbank.com

Subsidiary Company

MBSL Insurance Company Limited
No. 122, Kew Road
Colombo 02
Tel : 2 304500
Fax: 2 300499
E-mail : info@mbslinsurance.lk
Web : www.mbslinsurance.lk

Associate Company

Lanka Securities [Pvt.] Ltd
228/1, Galle Road
Colombo 04
Tel : 4706757
Fax: 4706767
E-mail : lankasec@sitnet.lk
Web : www.lsl.lk

Auditors

The Auditor General of the Democratic Socialist Republic of Sri Lanka

Lawyers

Julius & Creasy
Attorneys-at-Law, Solicitors & Notaries Public
No. 41, Janadhipathi Mawatha
Colombo 01

Principal Banker

Bank of Ceylon

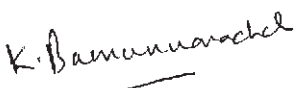
Notice of Meeting

NOTICE IS HEREBY GIVEN that the Thirty Sixth Annual General Meeting of Merchant Bank of Sri Lanka & Finance PLC will be held at the Grand Ballroom, Galadari Hotel, No. 64, Lotus Road, Colombo 01 on 26th June 2018 at 10.00 am for the following purposes;

1. To receive and consider the Annual Report of the Board of Directors and the Audited Financial Statements of the Company for the year ended 31 December 2017 together with the Report of the Auditors thereon.
2. To re-elect as a Director Mr. W P R P H Fonseka who retires by rotation in terms of Article 86 read with Article 87 of the Articles of Association of the Company.
3. To re-appoint the Auditor General as the auditor of the Company in terms of Article 154 [1] of the Constitution of the Democratic Socialist Republic of Sri Lanka for the financial year 2018. The Audit Fees for the audit shall be determined in accordance with Section 04 [Audit Fees] as stipulated in Public Finance Circular No: PED 01/2016 dated 01.01.2016.
4. To authorize the Directors to determine donations for the financial year 2018.

By Order of the Board of

MERCHANT BANK OF SRI LANKA & FINANCE PLC



K Jayatilake

Company Secretary

31 May 2018

Colombo

NOTES:

1. A Form of Proxy is attached hereto, for use if necessary, in which event, it should be completed and returned to the Registered Office of the Company – Bank of Ceylon Merchant Tower, No. 28, St. Michael's Road, Colombo 3 not less than 48 hours before the time appointed for the holding of the Annual General Meeting.
2. A Shareholder entitled to attend and vote at the Annual General Meeting is entitled to appoint a Proxy to attend and vote instead of him/her. A Proxy need not be a Shareholder of the Company.
3. The instrument appointing a Proxy may be in writing under the hand of the appointer or of his/her Attorney, or if such appointer is a corporation under its common seal or the hand of its Attorney or duly authorized person.

Form of Proxy

I/We.....

of.....

being a shareholder/ shareholders of the Merchant Bank of Sri Lanka & Finance PLC, hereby appoint

..... of..... whom failing

..... of whom failing any one of the Directors as *my/our Proxy, to represent * me/us, and to speak and to vote on *my/our behalf at the Annual General Meeting of the Company to be held at the Grand Ballroom, Galadari Hotel, No. 64, Lotus Road, Colombo 01 on 26th June 2018 at 10.00 am and at any adjournment thereof and at every poll which may be taken in consequence thereof. *I/We the undersigned hereby authorize my/our Proxy to vote on *my/our behalf in accordance with the preference indicated below:

| | For | Against |
|--|--------------------------|--------------------------|
| 01. To receive and consider the Annual Report of the Board of Directors and the Audited Financial Statements of the Company for the year ended 31 December 2017 together with the Report of the Auditors thereon. | <input type="checkbox"/> | <input type="checkbox"/> |
| 02. To re-elect as a Director Mr. W P R P H Fonseka who retires by rotation in terms of Article 86 read with Article 87 of the Articles of Association of the Company. | <input type="checkbox"/> | <input type="checkbox"/> |
| 03. To re-appoint the Auditor General as the auditor of the Company in terms of Article 154 (1) of the Constitution of the Democratic Socialist Republic of Sri Lanka for the financial year 2018. The Audit Fees for the audit shall be determined in accordance with Section 04 (Audit Fees) as stipulated in Public Finance Circular No: PED 01/2016 dated 01.01.2016. | <input type="checkbox"/> | <input type="checkbox"/> |
| 04. To authorize the Directors to determine donations for the financial year 2018. | <input type="checkbox"/> | <input type="checkbox"/> |

Signed this.....day of.....Two Thousand and Eighteen.

.....

Signature

Notes:

1. Please delete the inappropriate words.
2. If no indications are given and /or there is in the view of the proxy holder doubt [by reason of the way in which the instructions contained in the proxy form have been completed] as to the way in which the proxy holder should vote, the proxy holder shall vote as he /she thinks fit.
3. A proxy holder need not be a shareholder of the Company. A proxy so appointed shall have the right to vote on a show of hands or on a poll and to speak at the Meeting.
4. Instructions as to completion of the Form of Proxy is given below.

INSTRUCTIONS AS TO THE COMPLETION OF THE FORM OF PROXY

1. Kindly perfect the form of proxy after filling legibly your full name and address by signing in the space provided and filling in the date of signature.
2. Please indicate your preference with "X" in the appropriate cages provided in the form of proxy, as to how your proxy is to vote on the resolutions. If no indication is given the proxy in his / her discretion may vote as he / she thinks fit.
3. The instrument appointing a proxy may be in writing under the hand of the appointer or of his/ her Attorney, duly authorized in writing, or if such appointer is a corporation under its common seal or the hand of its Attorney or duly authorized person. If the form of proxy is signed by an Attorney, the relative Power of Attorney should also accompany the completed form of proxy, if it has not already been registered with the Company.

www.mbslbank.com