DFCC BANK PLC

Annual Report 2017

DFCC BANK

Keep Growing

Tea is a drink for anytime and DFCC is the Bank for the times

Vision

"To be the leading financial solutions provider sustainably developing individuals and businesses"

Mission

"To provide innovative and responsible solutions true to our Values with the expertise of our multidisciplinary team of professionals and synergies of our financial services group"

Our Values

Innovative
Customer Centric
Professional
Ethical
Accountable
Team Oriented
Socially Responsible

The new look DFCC Bank

"Pioneer, Pathfinder and Trailblazer"

DFCC is the First Bank to be listed in 1956 on the Colombo Brokers' Association, predecessor of the Colombo Stock Exchange and the second Financial Institution to do so. Its Shareholders span the gamut of local and foreign investors and include financial and non-financial corporates, investment funds, and individuals. Given below are highlights of the Bank's illustrious history from an investor's and a shareholder's perspective.

1955

DFCC founded by Act No. 35 of 1955 following World Bank initiative

Incorporated by an Act of Parliament; DFCC was the outcome of a joint effort by the Government of Sri Lanka and the World Bank consequent to the first World Bank mission in 1952

1956

Began operations with share capital of LKR Eight million; listed on the Colombo Stock Exchange with its shares held by eminent investors

Issue of 80,000 new shares at par value of LKR 100 to the public; over 70,000 shares subscribed to by institutions with the balance from individuals; subscribers included the Bank of Ceylon, National Bank of India, Indian Overseas Bank, National Mutual Life Association of Australia, HSBC and Grindlays Bank

1977 to 1979

New Share issues with International Financial Institutions coming on board

Staged issue of 160,000 new shares at LKR 100 to the public; IFC (the World Bank subsidiary), DEG (the German Development Bank) and FMO (the Dutch Development Bank) become investors in DFCC with each having a 10% shareholding

1983

Bonus Issue and New Share Issue increases paid-up capital

Bonus issue of 60,000 shares followed by issue of 700,000 new shares to the public increases the paid-up share capital to LKR 100 million

1991

Unprecedented demand for New Share Issue

Public issue of 366,667 ordinary LKR 100 shares at a premium price of LKR 500 oversubscribed by 19,000 new applicants; number of shareholders increased from 800 to 16,000

1992

Most valuable and profitable of companies listed on the Colombo Stock Exchange

Number one in market capitalisation on the Colombo Stock Exchange for three consecutive years; ranked first in profit after tax for listed companies

1995 to 1999

Best Managed Company in Sri Lanka for 1995 and the decade 1990/1999

Selected by "Asiamoney" financial journal as Sri Lanka's best managed company; recognised for "business strategy, financial management, fairness to minority investors and investor relations"

1998

Maiden International Note Issue guaranteed by a Multilateral Agency

Raised USD 65 million by the international issue of Floating Rate Notes guaranteed by ADB and listed on the Luxembourg Stock Exchange; ABN AMRO Bank was the Lead Manager to the issue

2003

Acquired commercial banking subsidiary

Acquired 94% of MERC Bank; revitalised, rebranded and re-launched as DFCC Vardhana Bank

2013

International Syndicated Loan and International Bond Issue demonstrates market acceptance and enhances profile among international investors

Raised USD 45 million via a debut international loan syndication among six foreign banks; HSBC was lead arranger and book runner for this transaction; also raised USD 100 million by the issue of an international five year bond listed on the Singapore Exchange – Citigroup Global Markets and Merrill Lynch (Singapore) acted as the Joint Lead Managers

2015

Re-incorporated as DFCC Bank PLC

Status changed from Public Quoted Company incorporated under Act of Parliament to Public Quoted Company incorporated under Companies Act No. 07 of 2007

2015

Amalgamated with DFCC Vardhana Bank

DFCC Bank and DFCC Vardhana Bank amalgamated; and is now a Licensed Commercial Bank

Contents

About this Report

This Integrated Annual Report serves as a disclosure of our strategy, governance, performance and prospects and how they help to create sustainable value within our operating environment.

Value Creation and Capital Formation

The value an organisation creates for its stakeholders and the ability of the organisation to create sustainable value for itself are mutually dependent activities – the more value the organisation creates, the more value it is able to create for itself. Therefore, firms spend substantial resources on creating and maintaining relationships with their stakeholders.

Value creation leads to capital formation. Capital is generally defined as wealth in the form of money and assets. In integrated reporting, capital takes on a broader definition: the resources and relationships used and affected by an organisation. We identify capital that is held by the organisation as being 'internal' capital, and capital not held by the organisation as 'external' capital. The aspect of ownership is irrelevant here as long as the organisation has access to and uses all forms of its capital to create sustainable value for itself and its stakeholders.

The structure of our Management Discussion and Analysis is based on value creation and capital formation.

Comprehensive and Yet Concise

Continuing with the approach to reporting adopted in the last three years, this Report balances the need to communicate effectively through concise, relevant information (to a large and diverse stakeholder group), while at the same time providing comprehensive compliance-related disclosures (that would interest only a few). We are thus presenting our Annual Report 2017 in three primary formats:

- A concise report (what you are now reading) in print and CD formats which meets compliance requirements while communicating with an audience looking for the essentials in an easily digestible format;
- A comprehensive report for a universal audience in online HTML format [http://dfcc2017.annualreports.lk] that includes our 'Perennial Compendium' feature, that tracks activities throughout the year which are relevant to our investors and stakeholders; and
- A condensed 'annual snapshot' in print and PDF formats that communicates across a broad spectrum of current and potential stakeholders.

Going beyond conventional reporting, we have implemented the latest Global Reporting Initiative (GRI) Standards format for reporting, an update to the GRI G4 format used in our previous annual reports. We continue to update our corporate website with a focus on investor relations, supplemented by an investor relations app for smart phones and other devices.

SCAN to view the online version
http://dfcc2017.annualreports.lk

Reporting Period

DFCC Bank Annual Report for 2017 covers the 12-month period from 1 January 2017 to 31 December 2017. The previous annual report covered the 12-month period from 1 January 2016 to 31 December 2016 and is available on the Bank website (www.dfcc.lk). One of the Group entities have a 31 March financial year-end and they are consolidated with DFCC Bank's reporting period with a three-month time lag. A summary of the accounting periods covered by the Statement of Profit and Loss and Other Comprehensive Income in the Bank and the Group columns is given in the Financial Reports (page 153).

Report Boundary

Our reporting covers DFCC Bank PLC ('DFCC Bank' or 'Bank') and the DFCC Bank Group ('Group') comprising the Bank and its subsidiaries, a joint venture company and an associate company. The respective entities are duly identified where applicable.

Compliance

As declared on page 149, the Board of Directors of DFCC Bank, in the spirit of good governance, accepts responsibility for the entirety of this Annual Report 2017.

The information contained herein, as in the past, is in compliance with all applicable laws, regulations, and standards. Additional details are given in the Corporate Governance Report (page 111), Financial Statements and Notes thereon (page 152) and the Independent Auditors' Report (page 151).

In addition, we have drawn on concepts, principles and guidance from the GRI Standards, the International Integrated Reporting Framework and the Smart Integrated Reporting Methodology™ in producing this Report.

Precautionary Principle

We take due cognisance of the social and environmental consequences of our actions, both direct and indirect. The latter are more significant and they arise from our lending operations, which are addressed through credit policies, the Social and Environmental Management System (SEMS), post-disbursement supervision, and risk management processes.

Comparability

The basis for reporting on subsidiaries, joint ventures and other entities, leased facilities, outsourced operations as well as any restatements and significant changes from previous reporting periods in the scope, boundary or measurement methods are disclosed where appropriate. They are in compliance with the reporting standards disclosed in the Financial Reports.

Queries

We welcome your comments or questions on this Report. You may contact the Company Secretary at our Head Office via post or email through the contact details given under Corporate Information.

Highlights

Financial Highlights

Group

LKR million	Year ended 31 December 2017	Year ended 31 December 2016	Nine months ended 31 December 2015	Year ended 31 March 2015	Year ended 31 March 2014
	Based on current SLFRS				
Operating Results					
Total income	**35,987**	26,980	17,503	20,094	20,376
Profit before tax	**5,891**	4,674	2,553	5,416	4,117
Tax expense	**1,458**	1,205	912	977	902
Profit attributable to equity holders of the Bank	**4,362**	3,415	1,592	4,362	3,151
Statement of Financial Position					
Assets					
Cash and short-term funds	**21,390**	13,824	9,870	9,471	10,913
Loans to and receivables from banks and other customers	**224,660**	198,085	164,945	138,887	117,716
Financial investments	**80,374**	72,461	66,861	56,699	40,976
Investments in associate and joint venture	**1,684**	1,443	1,248	1,188	1,029
Other assets	**6,360**	5,453	4,185	4,365	4,361
Total assets	**334,468**	291,266	247,109	210,610	174,995
Liabilities					
Due to other customers	**192,920**	140,220	110,551	92,712	80,917
Other borrowing	**84,578**	97,276	87,381	65,874	50,075
Other liabilities	**7,568**	6,660	5,208	3,761	3,549
Equity					
Total equity attributable to equity holders of the Bank	**49,125**	46,850	43,716	47,909	40,121
Non-controlling interests	**277**	260	253	354	333
Total equity and liabilities	**334,468**	291,266	247,109	210,610	174,995
Return on equity, %*	**12.08**	10.3	5.6	14.0	10.9
Return on total assets, %*	**1.47**	1.4	0.8	2.5	2.1
Earnings per share, LKR	**16.45**	12.88	6.01	16.46	11.89
Net asset value per share, LKR	**185.31**	176.73	164.90	180.72	151.34
Capital adequacy**					
Core capital ratio, % (Basel II)	-	14.60	15.39	17.71	18.71
Total capital ratio, % (Basel II)	-	17.47	15.32	16.62	17.19
Common equity tier I Capital ratio, % (Basel III)	**13.09**	-	-	-	-
Tier I capital ratio, % (Basel III)	**13.09**	-	-	-	-
Total capital ratio, % (Basel III)	**16.53**	-	-	-	-

** After eliminating fair value reserve.*
*** Reporting requirement for Capital Computation has been changed to Basel III with effect from 1 July 2017.*

Operational Highlights

Enhancing DFCC Virtual Wallet

Breaking new ground in Sri Lanka's banking industry, the DFCC Virtual Wallet is used by thousands of customers with over one thousand merchants. DFCC Chatz, an online chatbot, can be accessed via Facebook and provides instant feedback to customers and merchants. The Voice Command feature enables fund transfers, bill payments, and the ability to check account balances effortlessly.

Increasing Brand Visibility

The brand image/look and feel of a large number of branches were enhanced creating top of mind awareness for DFCC. The branches are situated at convenient locations island-wide, providing customers with an unmatched service.

Contributing towards a Sustainable Future

DFCC financed 18 renewable energy-based power generation projects with the capacity to generate 57 MW, with 16 projects operational by the end of 2017.

Embracing Technology to Drive Businesses

DFCC iConnect is an online portal built for DFCC Bank's Corporate, Business Banking and SME clients to carry out their daily transactions. It gives them the flexibility to access their portfolios at the click of a button.

Moving Towards a Sustainable Environment

Over seven thousand trees were planted across the country through eleven tree planting campaigns in Aranayake, Athurugiriya, Batticaloa, Beddagana, Bellanwila, Colombo, Jaffna, Kaduwela, Kahathuduwa and Thalawila.

Formulating Objective-Oriented Planning Strategy

DFCC's short term-three year plan (2018 to 2020) was formulated based on international best practices in line with the Bank's vision.

Receiving Global Recognition for Sustainable Initiatives

DFCC was honoured for "Outstanding Business Sustainability Achievement" at the Karlsruhe Sustainable Finance Awards. This Award honours financial institutions and organisations that have made significant contributions to the field of sustainable finance.

Launching DFCC Premier Go

DFCC's new "Premier Go" app was launched to empower Premier customers with the ability to view account balances, schedule appointments, keep track of their finances, get updated on current promotions and offers and connect to their dedicated Relationship Manager via video call anywhere in the world.

Message from the Chairman

The fundamentals have been put in place for stable, sustainable growth. This has been recognised by S&P and the international rating outlook has been revised to "stable" from "negative" while maintaining our ratings at B/B. Fitch also upgraded DFCC's international and long-term outlook from "negative" to "stable" while maintaining the international and domestic ratings at B+ and AA- respectively.

The Directors have approved a first and final dividend of LKR 5.00 per share, which is a payout of 32% of distributable profits.

The Bank has set itself a challenging target over the next three years, and our people are geared to bringing this plan to fruition.

SCAN to view the Message from the Chairman
http://dfcc2017.annualreports.lk/mftc.html

Dear Shareholders,

DFCC Bank has continued to grow in 2017. Our results show the dynamic is changing. Profit is up by 34%, expenses carefully managed despite the cost of relocating and upgrading branches and increased investment in building the DFCC brand. Our NPL ratio has come down to a historical low in line with industry average and CASA is slowly but steadily moving upwards.

We have been a great deal more visible than before as befits our commercial banking franchise, people are responding to our products, and our highly regarded customer service, with enthusiasm. During the year, the Bank has relocated many branches to more customer friendly locations with enhanced facilities and we have extended our digital footprint across cyberspace. Our Virtual Wallet now has thousands of users, with more merchants joining by the day, and it is fast becoming a necessity.

The fundamentals have been put in place for stable, sustainable growth. This has been recognised by S&P and the international rating outlook has been revised to "stable" from "negative" while maintaining our ratings at B/B. Fitch also upgraded DFCC's international and long-term outlook from "negative" to "stable" while maintaining the international and domestic ratings at B+ and AA- respectively. During a year within which the Bank had to face many challenges, this is a very significant achievement.

The Bank has set itself a challenging target over the next three years, and our people are geared to bringing this plan to fruition. Quarterly reviews of results against the plan are conducted at Board level, concerns identified and corrective action taken. Good corporate governance is a cornerstone of the Bank's policy and governance has been strengthened. The Bank recognises that our people are our greatest asset, and during the year under review, many initiatives to increase the skills and competence of the staff have been put in place, while ensuring they are well compensated, excellence rewarded, and talent recognised.

The Directors have approved a first and final dividend of LKR 5.00 per share, which is a payout of 32% of distributable profits. Shareholders will appreciate that with the introduction of Basel III, it is important that the Bank builds up its capital while ensuring shareholders get a fair return.

My thanks go out to the former CEO, Mr Arjun Fernando, and the current CEO, Mr Lakshman Silva for their untiring efforts to ensure the Bank performed creditably during the year, and to the Management team and staff at all levels who upheld the highest standards of professionalism and service that has enabled the Bank to produce these results. I am fortunate to have as colleagues on the Board a team of dedicated professionals whose guidance and support have been invaluable. I am grateful for the support of the officials of the Central Bank of Sri Lanka and the Ministry of Finance, and to our loyal customers for their continued patronage. We recognise that our customers are the reason for our success, and remain committed to providing a service that exceed expectations.

Mr Arjun Fernando relinquished duties as CEO on 15 August 2017, and I must acknowledge the huge contribution he made during his tenure. He was a driving force, along with Mr Lakshman Silva, behind the amalgamation with Vardhana, and the successful integration of the staff of the two banks. I wish Arjun every success in his future career.

Messrs Lalit Wijeyaratne, Ranjith Asoka and H A Ariyaratne left the Board during the year, and I thank them for their immense contribution, and wish them the very best. Ms Hiroshini Fernando joined the Board in November, and I have no doubt she will contribute greatly to Board deliberations. Mr Kithsiri Nemmawatta was appointed a Director on 1 February 2018, to succeed Mr Ranjith Asoka, and I welcome him to the Board.

You, our shareholders, have always been our strength and I thank you for your constant support over the years, and look forward to a continuation of this support in the years ahead, as we take your Bank forward and upward. With your support, we will ensure that DFCC Bank "keeps growing".

C R Jansz

Chairman

19 February 2018

Chief Executive's Review

Highlights of DFCC's financial performance speak volumes; advances and loan book up 15% to LKR 213,676 million, non-performing ratio down to 2.77% from 2.97%, deposits up 38% to LKR 193,308 million and profit after tax up 34% to LKR 4,415 million.

DFCC was the only commercial bank to have some form of upgrade during the rating period. The upgrades also reflect the fact that looking ahead, DFCC's strategies were acknowledged to provide the foundation for a sustainable progress.

While the Bank is regarded as a unique commercial banking institution with a development banking forte, it has also engendered an image for innovation.

SCAN to view the Chief Executive's Review
http://dfcc2017.annualreports.lk/cer.html

To be "the Bank for the Times" requires many things – it requires the institution to be at the cutting edge – to be customer centric, to be proactive to competitive pressures, to be attuned to channel developments, to explore "Blue Oceans" and so on. In other words, the institution must be agile on several fronts. The DFCC of today is progressing on a foundation based on capital strength and an agility fostered by four pillars – its employees, its financial technology, its franchise and a mindset of being a pioneer, a pathfinder and a trailblazer.

In 2017, DFCC was exemplified as the Bank for the Times. Following the amalgamation with DFCC Vardhana Bank and its transformation to a commercial bank in 2015, the new financial landscape might have proved daunting particularly given the fact that the Bank would be going head on against longer established commercial banks. However, it is gratifying that DFCC not only withstood the competitive pressure successfully but also prospered. This is validated by the highlights of DFCC's financial performance. Some key numbers speak volumes; advances and loan book up 15% to LKR 213,676 million, non-performing ratio down to 2.77% from 2.97%, deposits up 38% to LKR 193,308 million and profit after tax up 34% to LKR 4,415 million. In terms of the Group, the subsidiaries – Lanka Industrial Estates Limited and DFCC Consulting (Pvt) Limited posted profit growths as did the joint venture – Acuity Partners (Pvt) Limited. The IT Subsidiary – Synapsys Limited reduced its losses while the Associate – National Asset Management Limited recorded a small profit decline. Especially gratifying is the fact that the robustness of DFCC's performance was recognised by rating agencies S&P and Fitch. The former revised the Bank's international rating outlook to "stable" from "negative" while maintaining a B/B rating and the latter upgrading the Bank's international and long-term outlook to "stable" from "negative" while maintaining B+ and AA- ratings respectively. Moreover, DFCC was the only commercial bank to have some form of upgrade during the rating period. The upgrades also reflect the fact that looking ahead, DFCC's strategies were acknowledged to provide the foundation for a sustainable progress.

In the prelude to this message, there was reference to four pillars. As always, DFCC's greatest asset has been its employees and the increasing mix of young blood with the Bank's experienced cadre is a key factor enabling DFCC to quickly adapt to change and thereby move with the times. However, people need to be enabled to deliver, which is where DFCC's technology comes into play. An automated work flow and communication system has enhanced efficiency and virtually eliminated paperwork. On the delivery side, DFCC's Virtual Wallet, the first of its kind in the local banking industry, is rapidly gaining market acceptance. Another is an innovative Payments and Cash Management solution. With other products under development, DFCC is fully geared to embrace the Internet and Mobile banking regime. Together with people and technology, making headway in a crowded market also requires a strong franchise, including a regularly refreshed branding. During the year, DFCC stepped up its marketing initiatives and has raised its visibility. While the Bank is regarded as a unique commercial banking institution with a development banking forte, it has also engendered an image for innovation. Besides new products, the Bank remains as the financier of preference for pioneering ventures. Cases in point are two new waste-to-energy projects and a rooftop solar power programme. This appetite to venture boldly epitomises DFCC's mindset as a pioneer, pathfinder and trailblazer. In fact, over my 31 years at DFCC, I have personally witnessed how the Bank blazed a trail across the industrial and commercial landscape of Sri Lanka, from financing the first beach resort to being the first to venture into the financing of clean hydro, wind and solar energy. Eventhough all other banks were unwilling to take such long-term risks, DFCC forged ahead.

Going forward, DFCC has set in place plans to achieve a demanding target within the next three years. In doing so, it expects to be placed as a Systemically Important Bank in the upper quartile of commercial banks in Sri Lanka. A mix of complementary strategies will be employed, which would also include some "Blue Ocean" initiatives. In this context, DFCC will explore a range of opportunities in consolidation and offshore markets. The Bank will also leverage on its Group relationships particularly in the area of Public Private Partnerships.

In conclusion, I wish to express my appreciation for the guidance and inspiration provided by my Chairman, Mr Royle Jansz and other Board members. Their direction will continue to be invaluable in driving DFCC forward. My special thanks go out to Mr Arjun Fernando, my predecessor, who manned the helm till August 2017 and was the force behind the successful amalgamation between DFCC Bank and DFCC Vardhana Bank. I wish him well in his future endeavours.
I welcome on Board my deputy Mr Thimal Perera, who brings in a wealth of commercial banking expertise. I thank the Senior Management and my colleagues for their effort, which has enabled DFCC to reach a new performance threshold.
I thank all our customers for their loyalty and patronage.
I thank officials of the Central Bank of Sri Lanka, the Ministry of Finance and other Government authorities for their cooperation and support. I also thank the international financial institutions, our bondholders and debenture holders, and depositors for the trust placed in DFCC Bank. May they all continue to prosper from their relationship with the "Bank for the Times".

L H A L Silva

Chief Executive Officer/Director

19 February 2018

Board of Directors

10
Ms A Withana
Secretary to the Board

5
Ms S R Thambiayah
Director

6
K P Cooray
Director

1
C R Jansz
Chairman

2
L H A L Silva
Chief Executive Officer

7
Ms V J Senaratne
Director

8
Ms L K A H Fernando
Director

9
N K G K Nemmawatta
Director

3
P M B Fernando
Senior Director

4
T Dharmarajah
Director

1 — *C R Jansz*
Chairman

Appointed to the Board of DFCC Bank PLC in July 2010 and appointed Chairman in March 2014.

Mr Jansz presently serves on the Board of Melstacorp PLC, Distilleries Company of Sri Lanka PLC and other companies in the Melstacorp Group. He is a Director of Lanka Milk Foods (CWE) PLC, Lanka Dairies (Pvt) Limited and other companies in the Lanka Milk Foods Group.

He is a former Chairman of Sri Lanka Shippers' Council and a former member of the National Trade Facilitation Committee of Sri Lanka. He has many years of experience in logistics, and in documentation, insurance, banking and finance, relating to international trade.

Mr Jansz holds a Diploma in Banking and Finance from the London Metropolitan University (formerly London Guildhall University) – UK. He is a Chevening Scholar and a UNESCAP Certified Training Manager on Maritime Transport for Shippers.

2 — *L H A L Silva*
Chief Executive Officer

Appointed to the Board of DFCC Bank PLC in October 2015 and appointed as the Chief Executive Officer on 16 August 2017.

Mr Silva held the position of Deputy Chief Executive Officer since October 2015. He was the Chief Executive Officer and Executive Director of DFCC Vardhana Bank PLC from January 2010 to September 2015. Mr Silva started his professional career with the Department of Inland Revenue of Sri Lanka and joined the DFCC Banking Group in 1987. He was seconded to the service of DFCC Vardhana Bank in 2003 and functioned as the Chief Operating Officer of DFCC Vardhana Bank until his appointment as the Chief Executive Officer in January 2010.

Mr Silva is the Chairman of DFCC Consulting (Pvt) Limited, Lanka Industrial Estates Limited and Synapsys Limited, subsidiary companies of DFCC Bank PLC, and the Chairman of Lanka Ventures Limited, LVL Energy Fund Limited, as well as Lanka Financial Services Bureau Limited. He is a Director of Acuity Partners (Pvt) Limited, the joint venture company of DFCC Bank PLC, and a Director of Acuity Securities (Pvt) Limited and Sri Lanka Banks Association (Guarantee) Limited. Furthermore, he is a member of the Board of Directors of the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP).

Mr Silva holds a BCom (Sp.) from the University of Kelaniya and an MBA from the Postgraduate Institute of Management of the University of Sri Jayewardenepura.

3 — *P M B Fernando*
Senior Director

Appointed to the Board of DFCC Bank PLC in July 2013.

A former Partner of KPMG Ford, Rhodes, Thornton & Company, Mr Fernando has extensive experience in financial services.

He has functioned as the Group Finance Director of the Confifi Group and Finance Director for the Asia Region at Virtusa (Pvt) Limited. In 2005, he became the Managing Director of Capital Reach Group and was appointed as Director/Chief Executive Officer of Softlogic Finance PLC, following the consolidation of activities of Capital Reach Group under Softlogic Finance PLC.

At present, he is the Chief Executive Officer of Orient Finance PLC.

Mr Fernando holds a BSc in Applied Science from the University of Sri Jayewardenepura. He is a Fellow of The Institute of Chartered Accountants of Sri Lanka and a Fellow of the Chartered Institute of Management Accountants of UK.

4 — *T Dharmarajah*
Director

Appointed to the Board of DFCC Bank PLC in July 2014.

Mr Dharmarajah is the Senior Partner (Audit & Assurance) of Messrs Amarasekera & Company and serves as a Director of Raigam Wayamba Salterns PLC, Southern Salt Company (Pvt) Limited, Management Applications (Pvt) Limited, and DHS Medical Group (Pvt) Limited.

He is a Member of the Council of University of Sri Jayewardenepura and a member of the Standing Committee on Management Studies of University Grant Commission. He was a Director of DFCC Vardhana Bank PLC, a Member of the Board of Management of the Postgraduate Institute of Management, and Curriculum Development Committee of the National Institute of Education. He was also a Member of the Council of The Institute of Chartered Accountants of Sri Lanka.

Mr Dharmarajah holds a BSc in Management (Sp.) from the University of Sri Jayewardenepura and a Fellow Member of The Institute of Chartered Accountants of Sri Lanka, Association of Accounting Technicians of Sri Lanka, and Institute of Public Finance and Development Accountancy.

5 — *Ms S R Thambiayah*
Director

Appointed to the Board of DFCC Bank PLC in March 2015.

Ms Thambiayah is the Executive Chairperson of Renuka Hotels PLC and the Joint Managing Director of Renuka City Hotels PLC, of which she was the General Manager from 2001 to 2010, prior to assuming the current position with the Company. She is also a Director of Cargo Boat Development Co. PLC, Crescent Launderers & Dry Cleaners (Pvt) Limited, Renuka Consultants & Services Limited, Renuka Properties Limited, Lancaster Holdings Limited, and Portfolio Management Services (Pvt) Limited.

She was a Director of DFCC Vardhana Bank PLC from September 2012 to February 2015.

Ms Thambiayah holds a BA (Hons.) in Economics from the University of Nottingham, UK and a MMH from Cornell University's School of Hotel Administration, USA.

6 — *K P Cooray*
Director

Appointed to the Board of DFCC Bank PLC in March 2015.

Mr Cooray presently serves as the Chairman of Hotel Developers Lanka PLC and Associated Newspapers of Ceylon Limited, and as a Director of Synapsys Limited. He has held executive positions in several companies including Ceylinco Group, Richard Pieris Group, and the Maharaja Organisation.

He was instrumental in setting up Rivira Media Corporation (Pvt) Limited under the Richard Pieris Group and served there as founder Director and Chief Executive Officer. The two flagship newspapers launched under his direction, 'Rivira' and 'The Nation', continue to be widely read newspapers in Sri Lanka. During his tenure at Maharaja Group, he worked as a consultant, supervising, streamlining, and ensuring executive coordination of news broadcasts by the television and radio stations belonging to the Company.

Mr Cooray holds a BA (Hons.) in Political Science and Law from the University of Middlesex.

7 — *Ms V J Senaratne*
Director

Appointed to the Board of DFCC Bank PLC in July 2015.

Ms Senaratne presently holds the position of Chief Legal Officer and Company Secretary of Distilleries Company of Sri Lanka PLC and Company Secretary of Periceyl (Pvt) Limited. She is a Director of Paradise Resort Pasikudah (Pvt) Limited and Amethyst Leisure Limited, and an Alternate Director of Melstacorp PLC and Distilleries Company of Sri Lanka PLC.

She has 40 years of professional experience and is well versed in the fields of litigation, commercial law, conveyancing, and company secretarial practices. She held the position of Company Secretary at Sri Lanka Insurance Corporation PLC from May 2003 to 2009, and served as a Legal Officer at the Central Bank of Sri Lanka.

Ms Senaratne is an Attorney-at-Law and Notary Public, Commissioner of Oaths, having admitted to the Bar on 25 August 1977, and also a Solicitor of England and Wales.

8 — *Ms L K A H Fernando*
Director

Appointed to the Board of DFCC Bank PLC in November 2017.

Ms Fernando presently serves as the Chief Executive Officer/Executive Director of R I L Property PLC and a Director of Readywear Industries Limited, Foodbuzz (Pvt) Limited, R I L Trust Limited, United Motors Lanka PLC, TVS Lanka (Pvt) Limited, Unimo Enterprises Limited, Orient Motor Company Limited, and UML Heavy Equipment Limited. She also serves as the Chairperson of the Audit Committee of United Motors Lanka PLC.

She started her career at Kreston MNS & Co, a correspondent firm of Grant Thornton International – Sri Lanka Division, a firm of Chartered Accountants and counts over 20 years of professional and commercial experience in the fields of auditing, finance and management.

Ms Fernando is a Fellow of The Institute of Chartered Accountants of Sri Lanka and a member of the Institute of Certified Management Accountants of Sri Lanka.

9 — *N K G K Nemmawatta*
Director

Appointed to the Board of DFCC Bank PLC in February 2018.

Mr Nemmawatta is presently the Director General – Department of Public Enterprise, Ministry of Finance.

He has held several executive positions in the public sector. He has served as the Additional Secretary to the Ministry of Higher Education and Highways and the Ministry of Environment. He has also served as Director of Sri Lanka Samurdhi Authority, Sri Lanka Customs and Department of Trade, Tariff and Investment Policy.

Mr Nemmawatta holds a BCom (Sp.) from the University of Colombo. He also holds a Postgraduate Diploma in Devolution and Local Government Studies from the University of Colombo and an MSc in Management from the University of Sri Jayawardenapura. He is also a Licentiate of The Institute of Chartered Accountants of Sri Lanka.

10 — *Ms A Withana*
Secretary to the Board

Appointed as Secretary to the Board in May 2011.

She is also the Company Secretary of DFCC Bank PLC and a Director of Synapsys Limited. Ms Withana joined the Bank in April 1990 and has functioned as the Chief Financial Officer, Head of Operations, Head of Credit administration and Head of Accounting and Reporting.

Ms Withana was a Director of DFCC Vardhana Bank PLC from August 2003 to July 2012.

She is a former partner of a firm of Chartered Accountants and counts over 30 years of professional experience in the field of auditing, finance and management.

Ms Withana holds an MBA from the University of Colombo. She is a Fellow of the Institute of Chartered Accountants of Sri Lanka and a Fellow of the Chartered Institute of Management Accountants of UK.

Corporate Management

6
Bhathiya Alahakoon
Senior Vice President
(Branch Banking & SME)

7
Renuka Amarasinghe
Senior Vice President
(Corporate Banking)

8
Gillian Edwards
Senior Vice President
(Consumer Banking)

1
Lakshman Silva
Chief Executive Officer

2
Thimal Perera
Deputy Chief Executive Officer

3
Tyrone de Silva
Executive Vice President
(Strategic Planning & Subsidiaries)

9
Ashok Goonesekere
Senior Vice President
(Chief Financial Officer)

10
Achintha Hewanayake
Senior Vice President
(Chief Operating Officer)

11
Kapila Nanayakkara
Senior Vice President
(Treasury & Resource Mobilisation)

12
Rohitha Ganegoda
Senior Vice President
(Chief Information Officer)

4
Palitha Gamage
Executive Vice President
(Chief Risk Officer)

5
Anomie Withana
Executive Vice President
(Company Secretary/Secretary to the Board)

Management Team

21
Terrence Etugala
Vice President (Branch Manager – Gampaha)

22
Gaminda Fernando
Vice President (Services and Procurement)

23
Jayan Fernando
Vice President (Risk Policy and Modelling)

24
Chandana Garusinghe
Vice President (Branch Manager – Matara)

25
Nilmini Gunaratne
Vice President (Marketing)

26
Chaminda Gunawardana
Vice President (Regional Manager)

33
Saravanapavan Raveendra
Vice President (Regional Manager)

34
Mangala Senaratna
Vice President (Corporate Banking)

35
Sajith Silva
Vice President (Bancassurance)

1
Chinthika Amarasekara
Vice President (Finance)

2
Anton Arumugam
Vice President (Liabilities and Trade Business Development)

3
Pradeepa De Alwis
Vice President (Regional Manager)

4
Neville Fernando
Vice President (Business Systems)

9
Wajira Punchihewa
Vice President (Regional Manager)

10
Hemanatha Samaranayaka
Vice President (Head of Business Development)

11
Priyadarsana Sooriya Bandara
Vice President (Branch Credit Management)

12
Kapila Subasinghe
Vice President (Specialised Project Lending/Head of Consulting)

13
Pradeep Ariyaratne
Vice President (Regional Manager)

14
Shantha Atapattu
Vice President (Branch Manager – Kandy)

27
Samathri Kariyawasam
Vice President (General Legal)

28
Nalin Karunatileka
Vice President (Project Management and BCP)

29
Denver Lewis
Vice President (Alternate Channels and Cash Management)

30
Kelum Perera
Vice President (Branch Manager – Galle)

31
Thejaka Perera
Vice President (Litigation)

32
Nimali Ranaraja
Vice President (Business Banking)

36
Nishan Weerasooriya
Vice President (IT Operations)

37
Chandrin Wimaladharma
Vice President (Rehabilitation and Recoveries)

5
Sonali Jayasinghe
Vice President (Human Resources)

6
Charitha Jayawickrama
Vice President (Internal Audit)

7
Jayangani Perera
Vice President (Head of Business Banking)

8
Prasanna Premaratne
Vice President (Trade Services)

15
Priyadarshi Attanayake
Vice President (Business Banking)

16
Amanthi Balasooriya Dahanayake
Vice President (Credit Risk Management)

17
Gunaratne Bandara
Vice President (Regional Manager)

18
Subhashi Cooray
Vice President (Credit Administration)

19
Ravi Dassanayake
Vice President (Planning and Monitoring)

20
Ranjith Dissanayake
Vice President (Branch Manager – Kurunegala)

(10)
Dilshan Dodanwela
Assistant Vice President (Treasury Sales)

(11)
Roshan Eththiligoda
Assistant Vice President (Branch Manager – Negombo)

(12)
Prasad Fonseka
Assistant Vice President (Network Service Centre)

(13)
Asanga Goonatilaka
Assistant Vice President (Business Banking)

(14)
Gemunu Gunasumana
Assistant Vice President (Card Operations)

(15)
Shan Heenkenda
Assistant Vice President (Employee and Industrial Relations)

(22)
Rajaratnam Naguleswaran
Assistant Vice President (Correspondent Banking)

(23)
Sharmila Nugawela
Assistant Vice President (Legal – Business Operations)

(24)
Lakmal Rajasekara
Assistant Vice President (Branch Manager – Anuradhapura)

(25)
Ruwan Saram
Assistant Vice President (Branch Manager – Dambulla)

(26)
Kusumsiri Sathkumara
Assistant Vice President (Branch Credit Management)

(27)
Rasika Senaratne
Assistant Vice President (Retail Assets and Leasing)

(1)
Sumudu Abeygunasekara
Assistant Vice President (Corporate Banking)

(2)
Iranga Amilana
Assistant Vice President (Private Banking and Wealth Management)

(3)
Punitha Dahanayake
Assistant Vice President (Credit Administration)

(4)
Channa Dayaratne
Assistant Vice President (Resource Mobilisation)

(5)
Neil De Rose
Assistant Vice President (Branch Manager – Kotahena/ Bandaranayake Mw.)

16
Bhatika Illangarathne
Assistant Vice President (Branch Manager – Nawala)

17
Senaka Jayasinghe
Assistant Vice President (Sustainability)

18
Gayan Jayatissa
Assistant Vice President (Information Systems Security)

19
Iresha Kumbukage
Assistant Vice President (Credit Administration)

20
Jayanath Liyanage
Assistant Vice President (Rehabilitation and Recoveries)

21
Nilmini Mudalige
Assistant Vice President (Compliance)

28
Rohantha Seneviratne
Assistant Vice President (Specialised Project Lending/ Operational Manager DFCC Consulting)

29
Duminda Silva
Assistant Vice President (Retail Asset and Liability Sales)

30
Sudath Sovis
Assistant Vice President (Branch Manager – Nugegoda)

31
Chandana Wanigasena
Assistant Vice President (MSME)

32
Dushan Weerakoon
Assistant Vice President (PFS Central Processing)

33
Indaka Weerasekera
Assistant Vice President (Head of Payments and Settlements)

34
Niranjali Wijesinghe
Assistant Vice President (Branch Manager – Gampola)

6
Anuradha De Silva
Assistant Vice President (Branch Manager – Maharagama)

7
Nishani De Zoysa
Assistant Vice President (Corporate Banking)

8
Vidarsha Dharmasena
Assistant Vice President (Corporate Banking)

9
Pavithra Dias
Assistant Vice President (Branch Operations and Policies)

Organisational Overview

About DFCC Bank PLC

DFCC Bank PLC, originally established in 1955 as a Development Finance Institution on the recommendation of the World Bank, is one of the oldest development banks in Asia. The Bank is renowned for its project financing and SME financing expertise and has pioneered many new industries.

DFCC Bank and its 99% owned subsidiary, DFCC Vardhana Bank, amalgamated in October 2015. Today, DFCC Bank is a fully-fledged Licensed Commercial Bank offering the full gamut of development banking and commercial banking products and services.

DFCC Bank is rated AA-(lka) by Fitch Ratings (Lanka) Limited.

Group Structure

	Subsidiary company		Subsidiary company	
Name	DFCC Consulting (Pvt) Limited		Lanka Industrial Estates Limited	
Address	73/5 Galle Road, Colombo 3		LINDEL Industrial Estate, Pattiwila Road, Sapugaskanda, Makola	
Phone Nos.	+94 11 2442442		+94 11 2400318, +94 11 2400319, +94 11 2400320, +94 11 2400532	
Email	info@dfccbank.com		lindel@itmin.net	
Incorporated	9 September 2004		12 March 1992	
DFCC's Interest (%)	100		51.15	
Principal Activity	Consultancy		Operating an industrial estate	
Directors	L H A L Silva – Chairman S E de Silva (deceased 5 January 2018) T W de Silva		L H A L Silva – Chairman H A Samarakoon – CEO Mrs G M I U Bandara T W de Silva Dr R M K Ratnayake A D Tudawe	
Financial Year	2017	2016	2017/18	2016/17
Financial Year-End	31 December	31 December	31 March	31 March
Profit/(Loss) after Tax (LKR million)	1.7	(2.6)	146	111
Dividend per Share (LKR)	N/A	1.07	7.00	6.00
ROE (%)**	8	N/A	26	21

** Minority Interest*
*** Annualised*

Reach

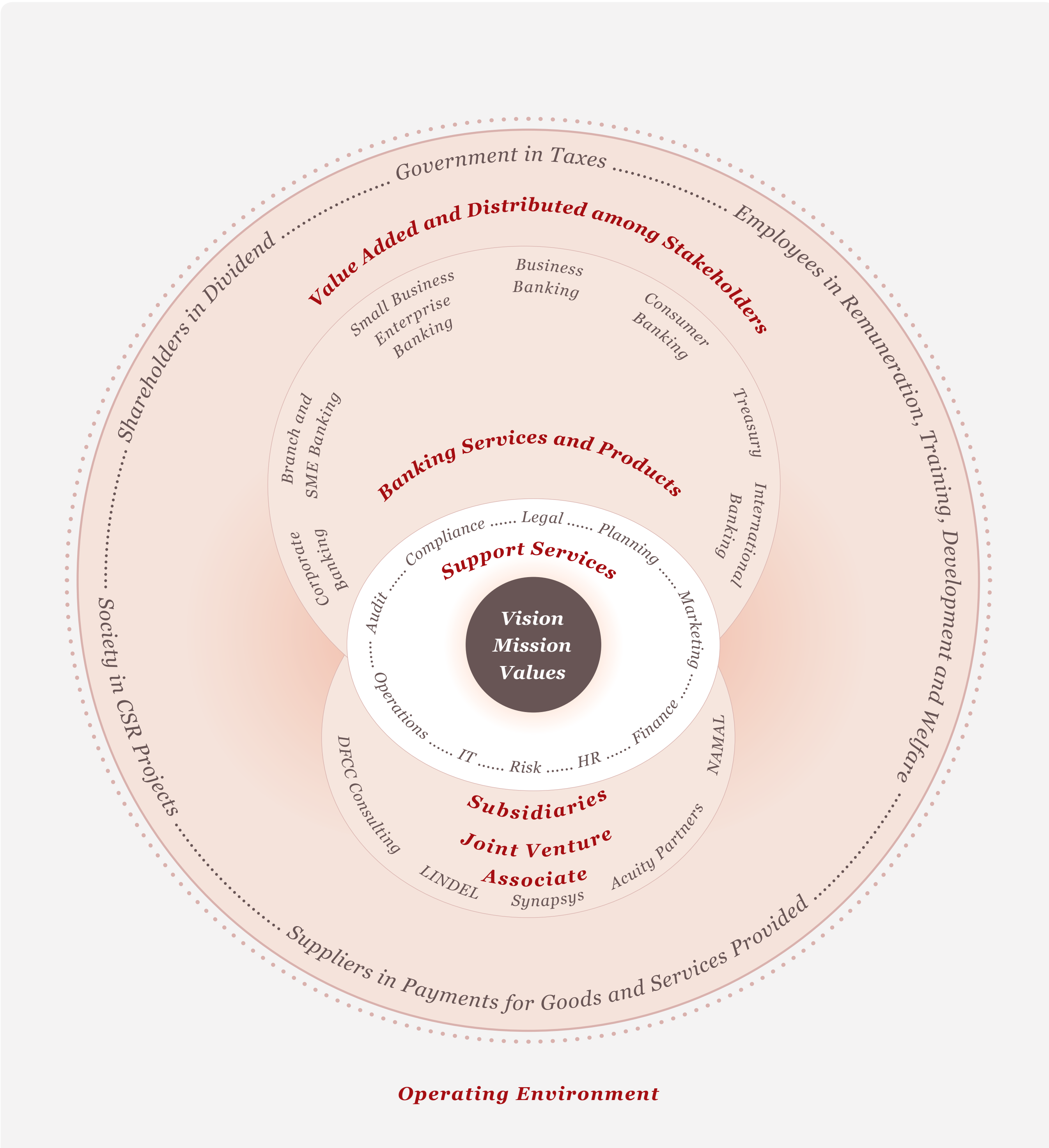
DFCC Bank delivers its services island-wide through 102 branches and 36 service points at Sri Lanka Postal outlets. Customers also have access to over 3,600 ATMs across the country via any LankaPay ATM network. DFCC Bank also provides Internet and Virtual Banking services through innovative digital technology.

Portfolio

DFCC Bank's primary lines of business are Corporate Banking, Branch and SME Banking, Micro, Small and Medium Enterprises, Business Banking, Consumer Banking, Premier Banking, Treasury, Institutional Banking and International Banking.

Subsidiary company		Joint venture		Associate company		
Synapsys Limited		Acuity Partners (Pvt) Limited		National Asset Management Limited		**Name**
540, Nawala Road, Rajagiriya		53, Dharmapala Mawatha, Colombo 3		7, Glen Aber Place, Colombo 3		**Address**
+94 11 2880702		+94 11 2206206		+94 11 2445911		**Phone Nos.**
contactus@synapsys.sg		info@acuity.lk		info@namal.lk		**Email**
11 October 2006		7 February 2008		28 September 1990		**Incorporated**
100		50		30		**DFCC's Interest (%)**
Information technology services and IT enabled services		Investment banking and related activities such as corporate finance, debt structuring and IPOs		Licensed unit trust and investment management		**Principal Activity**
L H A L Silva – Chairman D J P Fernandopulle – CEO K P Cooray G S Dewaraja T W de Silva N H T I Perera Ms R A P Withana		A J Alles – Chairman M R Abeywardena – CEO T W de Silva R Dissanayake D A B Ellepola D Pallewatte L H A L Silva		A Lovell – Chairman H A Herat – CEO Ms K S Bee W Dambawinne T W de Silva P Gamage S Madanayake M Samaratunga I Wickramasinghe		**Directors**
2017	2016	2017	2016	2017	2016	**Financial Year**
31 December	31 December	31 December	31 December	31 December	31 December	**Financial Year-End**
10.2	19.6	565 (Before MI)* 351 (After MI)*	535 (Before MI)* 299 (After MI)*	31	39	**Profit/(Loss) after Tax (LKR million)**
Nil	Nil	0.44	0.4	2.50	3.50	**Dividend per Share (LKR)**
N/A	N/A	10.44	10.1	14.25	18	**ROE (%)****

Our Business Model



Operating Environment

The Global Economy

The global economy continued the growth experienced towards the end of 2016. Global growth is estimated to have hit 3.6% in 2017, with growth in Europe, Japan, the United States, and Emerging Markets and Developing Economies (EMDEs) accounting for the improvement. The resurgence in growth of EMDEs played a role in improving the global economy, reaching an estimated growth of 4.6% in 2017. More moderate growth was experienced in advanced economies and China.

Going into 2018, the strengthening of the global economy is expected to continue, marking a growth of 3.7%. Pickups in investment, trade, and industrial production continue to be observed, and increasing confidence from businesses and consumers are aiding the recovery.

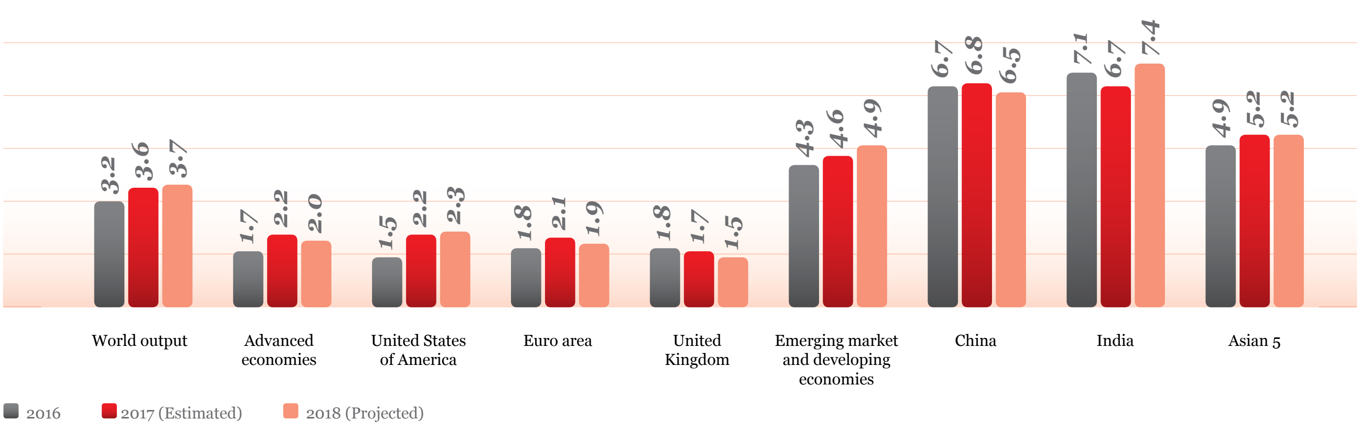
Advanced economies will likely experience a slight downturn in growth to 2.0%. Although performance was better than anticipated in 2017, the economic recovery is viewed as cyclical and expected to moderate. The potential growth of advanced economies will be affected by an ageing population slowing the growth of workforces, and productivity growth continuing its slow pace.

EMDEs are predicted to hit a growth rate of 4.9%, exhibiting a slower pace of growth and convergence than was seen in the past decade. Stronger projected activity in China and emerging Europe will primarily drive growth.

- The United States exhibited stronger-than-expected growth, despite challenging conditions, with a projected growth of 2.2%.
- Growth in the United Kingdom slowed down to 1.7%, due to Brexit-related uncertainty and inflationary pressures. The 2018 outlook looks uncertain as its economic relationship with the EU is redefined and barriers to trade, migration and cross-border financial activity are anticipated; growth is projected to fall to 1.5%.
- The Euro zone, benefitting from an increase in imports and stronger global trade activity, saw a projected growth of 2.1%. Growth is expected to moderate in 2018 at a projected 1.9%.
- China, a key investment partner of Sri Lanka, is projected to have grown at 6.8% due to improving global trade conditions and increasing household incomes and domestic demand. Growth is expected to moderate to 6.5% in 2018.
- Economic growth in India slowed to a projected 6.7% as the country continued to feel the effects of the currency exchange initiative launched in November 2016 and transition costs due to a countrywide Goods and Services Tax introduced in July 2017. The unification of India's domestic market and other key structural reforms are expected to improve growth to 7.4% in 2018.

Global Economy Highlights

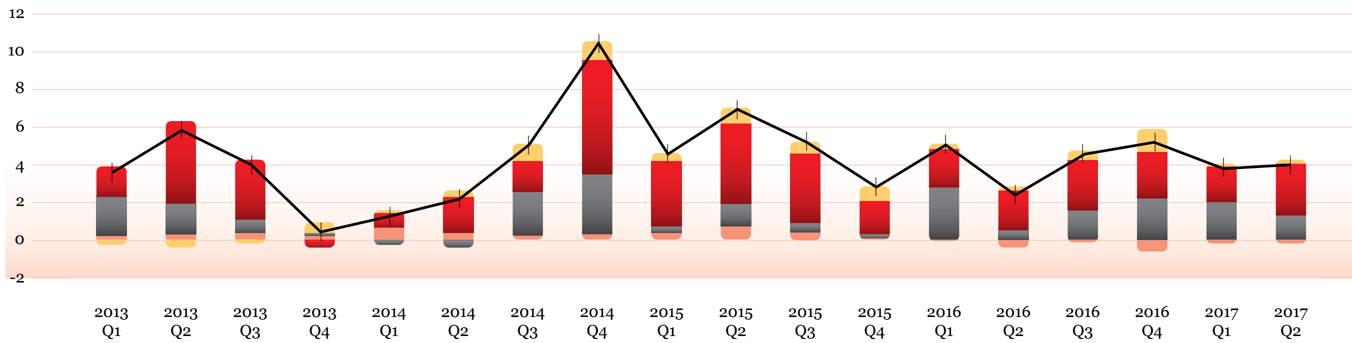
World Economic Outlook Projections – *(%)*



Source: World Economic Outlook

The Sri Lankan Economy

Quarterly Real GDP Growth (Year-on-year) – (%)



Source: The Central Bank of Sri Lanka

The Sri Lankan economy grew at a rate of 3.9% in the first half of 2017. The industry and services sectors propped up the economy, with the services sector turning in strong performances from financial services, wholesale and retail trade, and transportation. Adverse weather conditions continued to have a negative impact on the agriculture sector, which indirectly affected other sectors.

Positive momentum in investment and consumption expenditure contributed to GDP growth, and the country aims to take steps to keep the momentum going. With changes to the Foreign Direct Investment (FDI) Policy designed to attract investors from the US, China and India, Sri Lanka wants to seize its competitive advantages in location, skills base, and Free Trade Agreements, which the country is securing with developed and emerging markets.

Export earnings grew 7.6% year-on-year as a result of effective trade policies, a competitive exchange rate and the restoration of GSP+ concessions from the EU. Yet, increased rice and fuel imports, a result of the poor weather conditions, continued to widen the trade deficit. Imports expenditure grew 9.6% year-on-year.

The adverse weather conditions also contributed to inflation increasing to 8.6% (National Consumer Price Index, 2013=100) year-on-year in September 2017. Increasing international commodity prices and upward tax revisions led to inflation going well beyond the CBSL's 4-6% target.

The Sri Lankan Rupee depreciated 2.6% against the US Dollar (end November 2017). Increased import expenditure, debt service payments, and a reduction in foreign investments in Government securities contributed to the heavy outflows that impacted the currency. Further negative impact to the currency was stifled as a result of increased foreign investments to the Colombo Stock Exchange (CSE) and Government securities. The ongoing International Monetary Fund Extended Fund Facility (IMF-EFF) and the issuance of an International Sovereign Bond (ISB) further helped the Rupee weather the tough economic climate. The Rupee was further helped by the ongoing International Monetary Fund Extended Fund Facility (IMF-EFF) and the issuance of an International Sovereign Bond (ISB).

The Banking Sector

Sri Lanka's financial sector accounted for 9% of the country's estimated GDP in the first eight months of 2017. Profits after tax in the Banking sector grew 18.2% year-on-year.

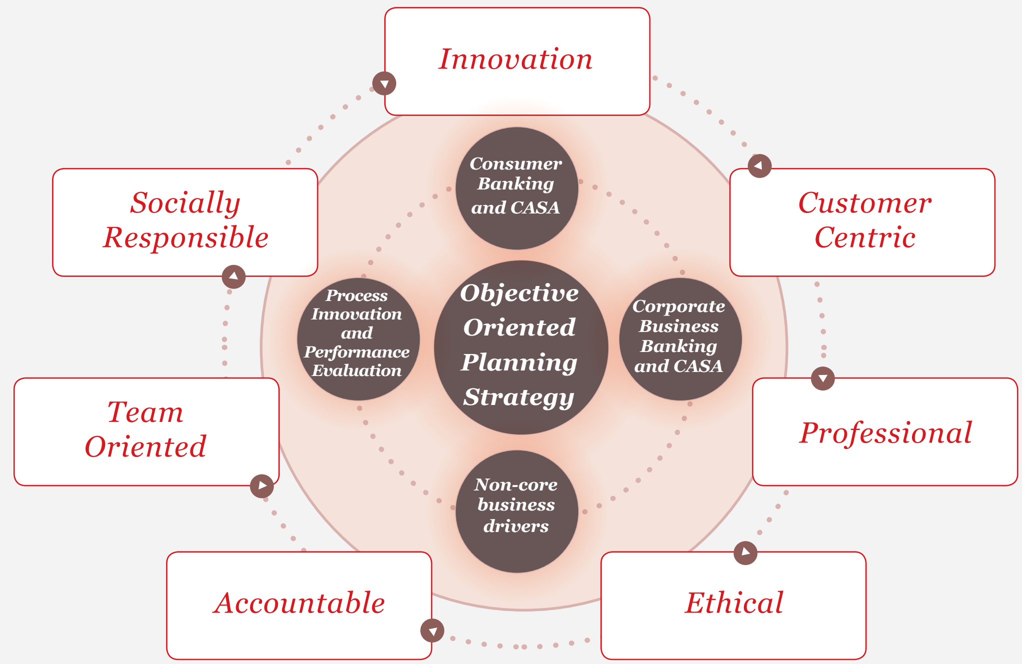
The sector grew its asset base by 9.4% during the first eight months of 2017. Deposits accounted for 71.3% of the total assets of the sector, and was a primary source of funding. Asset quality deteriorated slightly, but stability was maintained in the first eight months of the year as capital and liquidity levels were managed well above regulatory minimum requirements.

The CBSL raised interest rates, reducing the impact of the increased supply of money and high financing requirements on the Government budget. Despite this, lending to all economic sectors increased, increasing loans and advances to LKR 6.1 trillion (end August 2017), an increase of 10.8%. Macro-prudential policies implemented by the CBSL ensured growth in the leasing portfolio which was marginal at 3.1%. Increased net income, revaluation gains, and lower operating expenses contributed to the increased profitability of the sector.

Strategic Direction and Outlook

Short, Medium and Long-term Goals of the Bank

In keeping with the vision to be the leading financial solutions provider, the Bank set about formulating short, medium and long-term goals spanning from 2018 to 2020 and beyond. The Bank looked at its long-standing heritage of national development, the promotion of entrepreneurship and SME, and the recent move into the fully-fledged commercial banking space. The goals were formulated around the seven core values of the Bank and corporate planning sessions were arranged built on the pillars of Objective Oriented Planning Strategy (OOPS).



During the period 2018-2020, the Bank will focus on four main areas:

1. Consumer banking and Current Accounts and Savings Accounts share of wallet
2. Business banking and corporate banking share of wallet
3. Non-core business drivers to increase other income
4. Process innovation and performance evaluation

The Bank intends to maximise resource utilisation towards improving the customer experience and offering better customer convenience, including improving the digital customer experience in order to achieve customer satisfaction, retention, loyalty and engagement.

In an effort to broaden the customer base of the Bank, a number of strategic initiatives derived through OOPS have been established in different customer segments. Some of these initiatives include user-friendly online banking solutions and actively engaging customers through more loyalty building activities across customer touchpoints. As part of the OOPS initiative, a re-evaluation of the current business model of the Bank was undertaken, based on a nine building block analysis technique. This includes analysis of customer segments, value propositions, channels, customer relationships, revenue streams, key resources, key activities, key partners, and cost structures in order to shift the Bank's perspective from organisation-centric to customer-centric.

In general, the Bank focuses on enhancing productivity at branch level while reducing the paperwork of day-to-day operations in an effort to move towards a modern paperless work environment and establish a sustainable green banking solution. As measures of improved business processes, the Bank intends to implement the principles of lean management, truly paperless processes, improved workflow tools and automated task management.

Additionally, the Bank intends to improve MIS and innovation while focusing on customer profitability, employee motivation and engagement. The Bank plans to carry out marketing and promotional activities in the city and rural areas with the objective of raising brand awareness and creating a strong position in the minds of consumer banking customers.

SWOT Analysis

Strengths	Weaknesses
→ Solid reputation in the industry with a strong heritage → Multidisciplinary staff → Recognition from international funding agencies → Expertise in energy sector → IT subsidiary that provides Fintech solutions → High equity base → Previous experiences in transforming entities: DFCC Vardhana Bank, National Asset Management Limited, Lanka Ventures Limited, Lanka Industrial Estates Limited etc.	→ Low number of current accounts and savings accounts/small ticket deposits → Limited presence in trade opportunity areas → Limited operations in Foreign Currency Banking Unit (FCBU)/Export clients → Low customer reach → Attractiveness of the offerings – Credit cards offers and loyalty programmes → Inadequate footprint in Western Province → Lower cross selling ratio → Limited overseas presence → Higher concentration of existing customers on traditional project lending

Opportunities	Threats
→ Customer-centric business models → Business intelligence and information advantage → Opportunity to tie up with local agents → Untapped potential in Foreign currency business → Consultancy business → Entrepreneur incubator model → Supply chain funding solutions	→ Cyber security → BASEL III capital adequacy requirement → Maintain the existing rating → Expected political and economic disruptions → Increasing cost of existing and new foreign debt and premium on swap → Challenges from non-banking institutions eg: Telcos → Increasing concentration of business ownership → Consolidation move

Stakeholders

The individuals and organisations we interact with on a continuous basis are influenced by the activities we engage in as we assume the roles of a bank, an investor, an employer, and a business partner. Likewise, the actions of these individuals and organisations also influence our business. These are our stakeholders, and by adhering to our seven core values, we focus on building healthy and sustainable relationships with each other.

Stakeholder Engagement

We firmly believe that the relationships we build with our stakeholders are key to our success. Therefore, engaging with our stakeholders in a meaningful and consistent manner is a fundamental part of our decision making processes, and fulfilling our commitment towards responsible and sustainable value creation. We engage with our stakeholders via various means and at a frequency best suited to each stakeholder group, as described below.

Investors

The nature of our business is capital-intensive, and our investors help to ensure our continued growth by providing equity and debt capital. Our responsibility to our investors is to ensure that our growth offers them optimal returns on their investments.

Our Board-approved Corporate Communications Policy ensures that our investors are able to make well-informed decisions about investments in the Bank. Information about our financial performance and progress is made publicly available through the Colombo Stock Exchange (CSE), and is also communicated through our Annual Report, press and media releases, and our website. Every effort is made to convey context and insight on the Bank's value creation process.

We primarily communicate with our investors through our Annual Report, the Annual General Meeting, the corporate website, Stock Exchange announcements, press conferences, media releases, the investor relations hotline, meetings, and teleconferences. Key issues debated through these channels include Board governance, sustainable performance, and initiatives to improve shareholder returns.

Customers

Customers are the source of our earnings, and we exist to serve them. The relationship we share with our customers necessitates that we understand their evolving needs and requirements, in order to provide them with a relevant and comprehensive portfolio of financial products and services.

Understanding the interests and concerns of our customers helps us to provide better products and services, terms and conditions, tariffs, service standards, and financial advice. We engage with our customers through our front-line staff, relationship managers, advertising and promotion, media releases, branch personnel, our corporate website and social media platforms, alternate channels, the call centre, surveys, and other automated services.

Employees

Our employees form the backbone of our organisation; they espouse our core values (refer to Institutional Capital on page 51), and it is through them that we achieve our mission and fulfill our vision. We strive to ensure that they are fostered, inspired, and rewarded for their efforts and contributions to our organisation.

The Bank's internal Code of Conduct is accessible to its employees via the internal web portal. The Code of Conduct lays out our business ethics in relation to avoidance of conflicts of interest, insider dealings, unfair business practices, and the confidentiality of sensitive information.

A Whistleblowing Policy is also in place to encourage employees to report any observations of illegal or unethical practices. A Board-approved Grievance Handling Policy and procedure ensures that employees are provided with a fair, successful and productive workplace environment.

We engage with our employees through meetings, performance reviews, the human resources intranet portal, email bulletins, the weekly newsletter, training workshops and seminars, special events, employee surveys, the suggestion box, and grievance procedures.

Business Partners

Our business partners include institutions that provide lines of credit (to manage or to on-lend) and vendors that provide goods and services required for business operations; they are an important constituent of our value chain. With their support and participation, we create sustainable value.

Our international financiers are interested in the progress of programmes financed, social and environmental management practices, compliance, overall health of the Bank, and the latest developments and opportunities. We engage with our business partners through electronic exchanges of information, teleconferences, and participation in review missions.

Where our suppliers are concerned, a Board-approved Procurement Policy has been established. Discussions with suppliers primarily revolve around quality, reliability and pricing, while building mutually rewarding long-term relationships.

Regulators

Regulators protect and enhance the country's financial system through the implementation and enforcement of rules and regulations. By combatting financial crime and protecting consumers, regulators increase market confidence that benefits all involved parties. We abide by these rules and regulations by complying with all applicable legal and regulatory requirements, and conducting our business in an ethical, transparent, and responsible manner.

Discussions with regulators often cover compliance with regulations, business operations, financial information pertaining to the Bank, voluntary guidelines and best practices, new legal and regulatory developments, financial inclusion, and matters affecting the financial sector. In addition to directly engaging with regulators, we also engage with them through industry bodies, through the timely submission of prescribed reports and returns, participation in meetings, forums, task forces, and conferences, as well as media releases and the corporate website.

Society and Environment

The communities we operate in are a source of customers and employees. Therefore, it is our duty to understand their perceptions and expectations of us, and mould our operations and CSR initiatives around them in order to foster mutually beneficial partnerships.

We engage with our local communities through our network of branches and public events. We support them through volunteer efforts and CSR activities that cover entrepreneurial development, education, environment conservation, emergency relief, and sponsor deserving causes. Furthermore, we engage with the media through meetings, press conferences, press releases, and our corporate website.

External Interactions

DFCC Bank is a member of several associations and organisations, and our staff actively participate in activities coordinated by these institutions. Refer to Business Partner Capital on page 75 for a list of industry associations and organisations that DFCC Bank has obtained membership in or established affiliations with.

Materiality

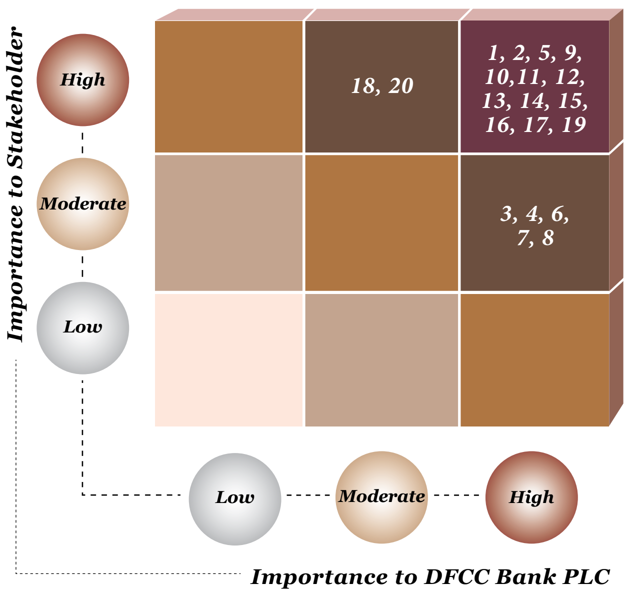
Materiality and Value Creation

The Bank considers materiality when formulating any strategic directions or priorities – that is, any economic, social, and environmental aspects that have an influence on its ability to create sustainable value.

These aspects are considered to be material if they are both relevant and significant to our stakeholders and to the Bank. Significance considers the magnitude of the impact of these aspects, as well as the likelihood of their occurrence.

Materiality Matrix

As part of our materiality analysis, we have determined aspects that are of importance to our stakeholders and to the Bank with regard to our economic, social and environmental agenda for sustainable value creation. These have been mapped on the GRI Standards two-dimensional matrix.



Details of the GRI content index are given in the online report
http://dfcc2017.annualreports.lk/gri.html

No.	Category/Topic
1.	Economic performance
2.	Market presence
3.	Indirect economic impacts
4.	Procurement practices
5.	Anti-corruption
6.	Energy
7.	Emissions
8.	Environmental compliance
9.	Employment
10.	Occupational health and safety
11.	Training and education
12.	Diversity and equal opportunity
13.	Non-discrimination
14.	Freedom of association and collective bargaining
15.	Child labour
16.	Forced or compulsory labour
17.	Local communities
18.	Marketing and labelling
19.	Customer privacy
20.	Socioeconomic compliance

Management Approach

Through effective engagement with our stakeholders, we are able to map a portfolio of strategies. With the careful execution of these strategies, the Bank and the Group are able to generate and deliver value to its stakeholders, and derive value in turn. This process helps to accomplish the strategic goal of certifying the sustainability of operations of the Bank and the Group. It also helps the Bank to establish durable relationships with customers, empower employees with mutually rewarding careers, generate steady returns for investors, establish mutually beneficial and profitable partnerships with partners and act responsibly towards the society and the environment.

The Management Discussion and Analysis section discusses the initiatives undertaken during the review period in further detail. These initiatives are classified as internal and external capital, taking into consideration the context of the operating environment and the strategic direction.

Changing with the times...

From a largely manual platform, the banks of today are fast evolving to a digital platform.

Likewise, DFCC has progressed technologically with many groundbreaking products such as the DFCC Virtual Wallet, Premier Go and DFCC i-Connect.

This exemplifies the Bank's willingness to embrace new technology, transform its culture, service and product offerings, thereby effecting the change that comes with the times.

Value Creation and Internal Capital Formation

Internal capital is the reciprocal value generated by the Bank and the Group – through activities, relationships, and linkages with the various stakeholders – for its own benefit. This capital consists of financial and institutional capital: financial capital is quantifiable and is represented in the Group's financial statements, and institutional capital is represented by abstract entities such as organisational knowledge, systems and processes, corporate culture and values, brand equity, business ethics, and integrity and associated collateral. The combination of these capitals help us to deliver greater value to our stakeholders, and we strive to grow these capitals further.

FINANCIAL CAPITAL

Financial Performance

Overview

DFCC Bank ended the year 2017 accomplishing many significant milestones after completing its second year as a fully-fledged commercial bank. During the year S&P Global Ratings and Fitch Ratings Lanka Limited upgraded DFCC Bank's outlook from "Negative" to "Stable". Fitch Ratings affirmed the National long-term Rating AA- and S&P Global Ratings affirmed 'B' long-term and 'B' short-term credit ratings on DFCC Bank. The total asset base of the Bank grew by 15% year-on-year to LKR 333,107 million with the Loans and Receivables exceeding the LKR 200 billion mark to end at LKR 213,676 million. The deposit base improved prominently by 38% to LKR 193,308 million with CASA (Current and Savings deposits) recording a remarkable increase of 45% year-on-year. The ratio of CASA over the total deposits improved to 21.5% by end 2017. The Bank's NPL ratio improved to 2.77% from 2.97% in 2016.

Continuing its commitment to financial inclusivity, the Bank added a branch in the Western Province and 14 extension offices were converted into fully-fledged branches during the year in line with its geographical expansion drive and achieved a total branch network of 138.

Profitability

The Bank recorded a profit before tax of LKR 5,792 million, a growth of 31% and profit after tax of LKR 4,415 million, a growth of 34%. The Group recorded a profit before tax of LKR 5,891 million, a growth of 26% and a profit after tax of LKR 4,434 million, a growth of 28%. This performance amply demonstrates the Bank's ability to consolidate its position as a commercial bank within a short period.

Net Interest Income

The Bank's total income for the year 2017 recorded an increase of 34% to LKR 35,942 million. The interest income consists of 92% of the total income of the Bank. The growth of LKR 6,230 million in interest income from loans and receivables from other customers mainly contributed for this growth. The Bank's net interest income recorded a credible growth of 27% to LKR 11,343 million from LKR 8,901 million in 2016. Interest margin increased to 3.64% from 3.32% in December 2016. This performance is commendable given the significant growth of LKR 40,231 million in fixed deposits during the year. Close monitoring of market trends and repricing of assets and liabilities at correct intervals helped to achieve this result. The total interest income grew by 36% to LKR 32,987 million. Interest expenses increased by 42% to LKR 21,644 million mainly due to 38% increase in the deposits due to other customers.

Fee and Commission Income

Growth in overall business segments, introduction of new products based on changing needs of customer profile and expanding delivery through electronic channels and other means helped the Bank to record a 22% growth in net fee and commission income. Fees generated from loans and advances and from services provided through customer accounts accounted for the majority of the increase. Fees collected from trade-related services, remittances, issue of Guarantees and Bancassurance services grew during the year. The Bank's credit card income recorded a moderate growth. The Bank initiated the issuing of credit cards from its own system from December 2017. This move would add more value to the customer convenience and will open up considerable growth in earnings from this important business line.

Total Operating Income

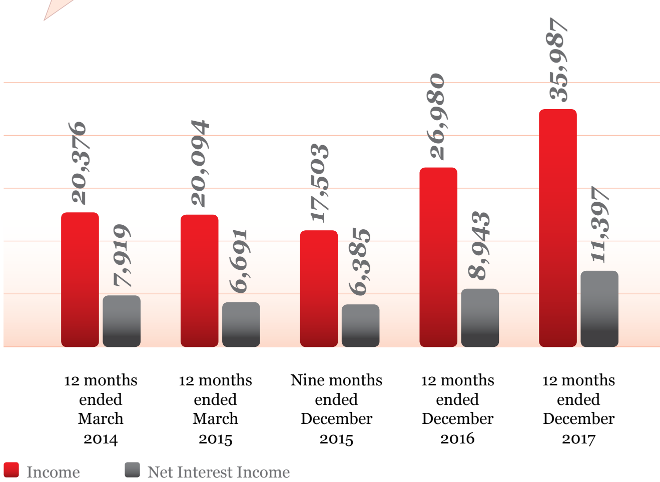
Net gains from trading of FOREX, fixed income securities and equity trading increased by 6% to LKR 362 million.

During the year, the Bank's swap book increased substantially due to increase (net) in foreign borrowings and foreign currency deposits during the year. The incremental premium cost due to the volume increase and marked-to-market fair value changes mainly contributed to the losses reported in both "net loss from financial instruments at fair value through profit and loss" and "other operating loss". The increased cost is however recovered through higher interest income earned from rupee lending funded through swaps.

Net gain from financial investments recorded a substantial growth of 92% (LKR 1,073 million) mainly from the sale of 10,024,888 shares from investment of 14.7% stake in Commercial Bank of Ceylon PLC shares. The sale proceeds were used to purchase shares allotted through the rights issue. The overall positive growth in total revenue streams contributed to 25% increase in total operating income to record LKR 14,298 million from LKR 11,461 million in the year 2016.

Total Group operating income increased by 23% to LKR 14,390 million from LKR 11,717 million reported in the previous year.

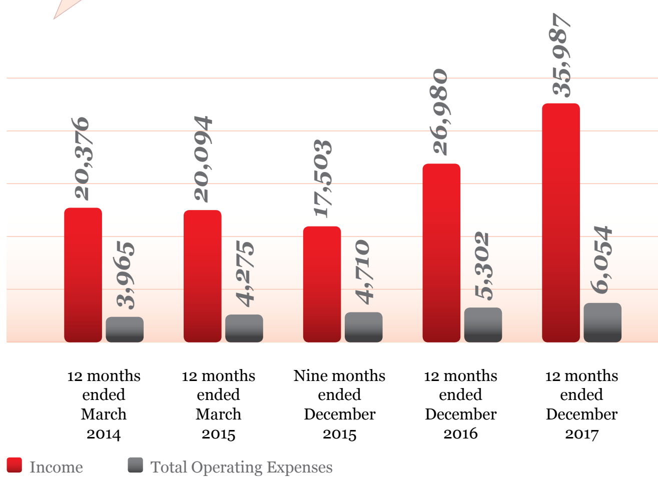
Income (Group) – *LKR million*



Impairment Charge on Loans and Other Losses

The impairment charge for the year increased by 26% mainly from the increase in collective impairment by LKR 324 million. This increase came from the growth in loans and receivables from other customers. The specific allowance for impairment declined by 8% to LKR 724 million from LKR 792 million in the year 2016. Continuous monitoring and timely corrective measures helped the Bank to curtail overdue loans. Consequently, the Bank's ratio of non-performing advances (NPA ratio) improved to 2.97% at the end of 2017 from 2.77% in December 2016. There was no change in the methodology adopted in computing collective impairment and specific impairment on individually significant loans during the year.

Total Income and Operating Expenses (Group) – *LKR million*

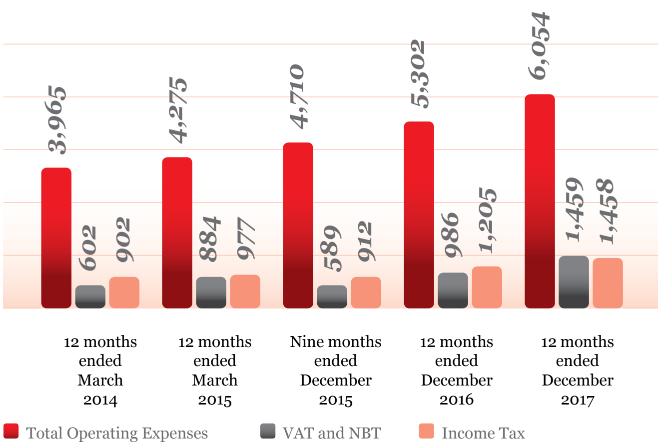


Operating Expenses

The Bank's strategy in increasing its franchise through expansion of sales forces was aggressively adopted during the year. The increase in branch network, expansion of product base and creating multiple delivery channels through automation contributed to increase in revenue streams, deposit growth and customer base. The incremental cost that had to be incurred for the above business growth mainly contributed to 15% increase in operating expenses. However, careful monitoring and effective cost control measures adopted during the year along with additional revenues generated during the year helped the Bank to record a lower cost to income ratio of 41.1% in 2017 compared to 44.7% in the previous year.

The Group operating expenses increased by 14% to LKR 6,054 million from LKR 5,302 million in the year 2016.

Expenses (Group) – *LKR million*



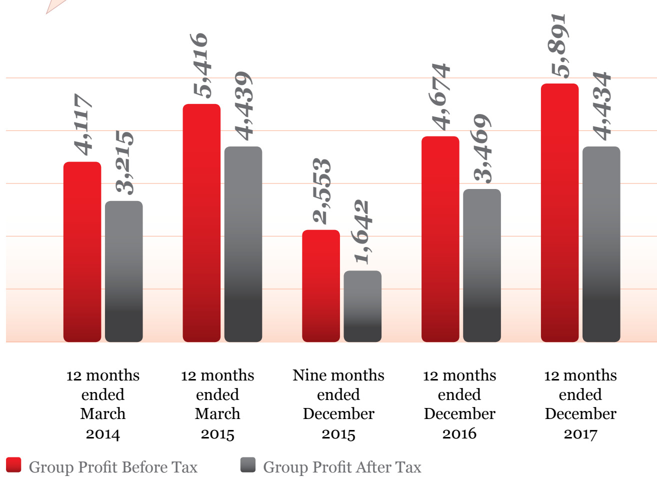
Profit Before Tax (PBT)

The profit before tax of the Bank increased by 31% for the year 2017 to record at LKR 5,792 million from LKR 4,414 million in the year 2016. The tax rate for financial VAT increased to 15% from 11% during the year 2016. When the tax increase is adjusted for the full period of 2016, the profit before tax of the Bank for the year 2017 had actually grown by 37% year-on-year. The Group profit before tax increased by 26% to LKR 5,891 million during the year 2017 from LKR 4,674 million in 2016.

Profit After Tax (PAT)

The Bank reported a profit after tax of LKR 4,415 million, a growth of 34% from LKR 3,289 million in the year 2016. The Group profit after tax attributable to equity holders of the Bank increased by 28% to LKR 4,362 million compared to LKR 3,415 million in the year 2016.

Group Profit Before and After Tax – *LKR million*



Financial Position Analysis

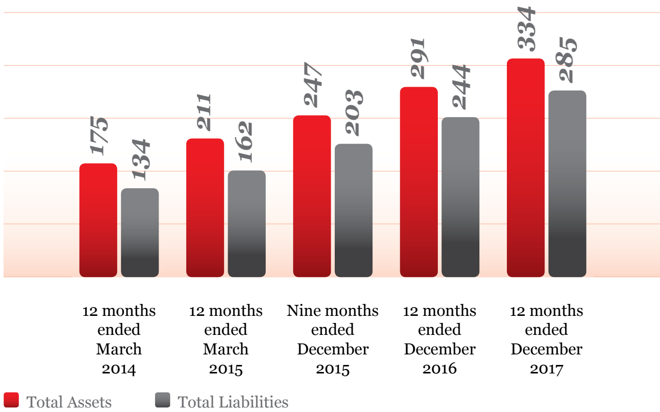
Assets

The Bank's total asset base as at 31 December 2017 grew by 15% to LKR 333,107 million from LKR 290,060 million as at 31 December 2016. The growth of the asset base was accounted mainly from the growth of LKR 27,891 million in loans to other customers, LKR 9,323 million from Government bills and bonds, and LKR 5,340 million in placements with Banks. The term loans growth of LKR 12,691 million recorded the highest out of the total growth in loans and receivables from other customers, followed by overdrafts (LKR 11,089 million) and trade finance (LKR 5,051 million).

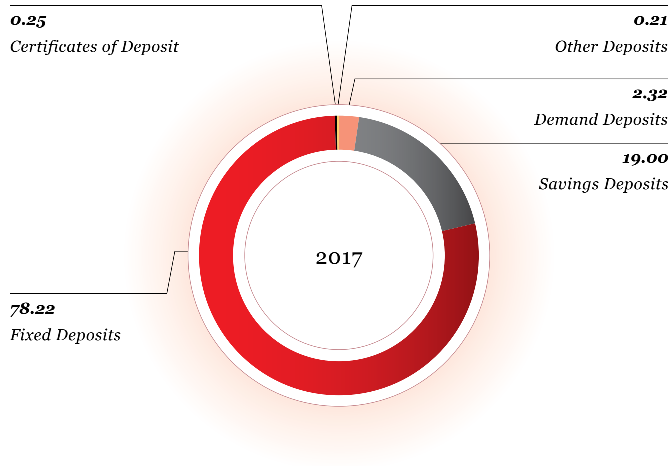
Despite regulatory constraints and increased vehicle market prices during the year, the leasing receivables (net) increased by LKR 584 million. The pawning advances had a growth of LKR 487 million during the year.

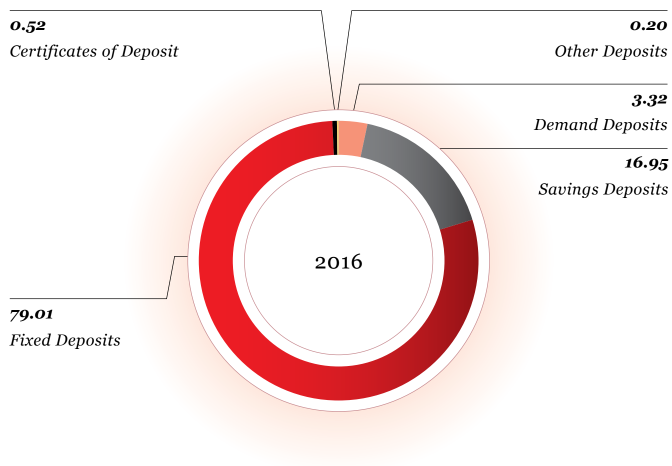
The Bank being the major contributor to the asset base, the Group total asset base increase was the same as that of the Bank.

Assets and Liabilities (Group) – *LKR billion*



Deposit Mix (Group) – *%*





Liabilities

The Bank was able to record a substantial growth of 38% in its deposit base during the year. This growth brought up the deposit base to LKR 193,308 million from LKR 140,514 million (2016) as at December 2017. The Bank's loans to deposit ratio improved to 114% from 137% as a result. The Bank undertook very successful promotional campaigns on low cost deposits during the year that helped to increase its current and savings deposits (CASA) by 45%. Total CASA deposits increased by LKR 12,682 million to LKR 41,129 million compared to LKR 28,448 million as at end 2016. This improved the CASA ratio to 21.3% from 20.2% in 2016. The Bank will continue to grow this segment aggressively during 2018. Foreign currency deposits of the Bank also recorded a significant growth of 47% to LKR 41,755 million from LKR 28,346 million year-on-year.

The Bank reduced its short-term borrowings substantially during the year by growing its deposit base. Accordingly, balances due to Banks declined by 47% to LKR 9,641 million from LKR 18,104 million as at end 2016. DFCC Bank continued its approach to tap local and foreign currency related, long to medium term borrowing opportunities. This has increased other borrowings by LKR 568 million (net) during the year under review. The Bank was able to settle its Debenture of LKR 5,000 million matured during the year. This brought down the Debt securities issued by LKR 4,735 million to LKR 24,444 million from LKR 29,179 million year-on-year. Due to the increase in business volumes, Bank's other liabilities increased by LKR 275 million (7%).

Equity and Compliance with Capital Requirements

The Bank's total equity increased by LKR 2,027 million during the year from the addition to retained earnings.

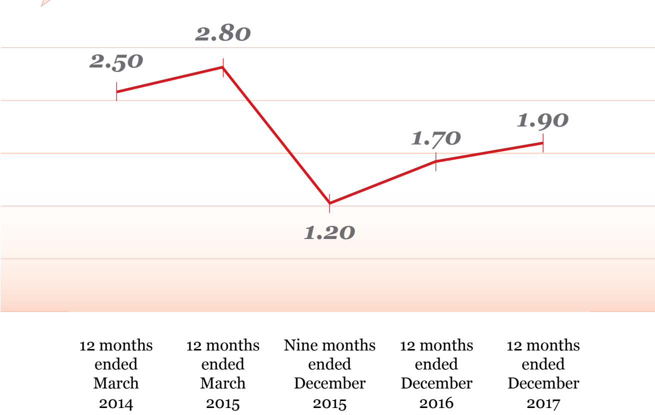
The Bank's profit for the year of LKR 4,415 million was lowered to LKR 3,199 million in total comprehensive income mainly due to the transfer of LKR 1,189 million from Other Comprehensive Income to Profit and Loss account on account of sale of shares in investment of Commercial Bank of Ceylon PLC (Refer Total Operating Income above). There were net gains from the change in fair value of available-for-sale financial assets and actuarial gains and losses from defined benefit plans totalling to LKR 239 million during the year.

The basic earnings per ordinary share of the Bank increased by 34% to LKR 16.65 from LKR 12.41 in the year 2016. The Bank's Return on Equity (ROE) improved to 9.4% from 7.4% in the year 2016. The Bank's Return on Assets (ROA) before tax increased to 1.9% from 1.6% in the previous year. Bank's net asset value per share was up by 4% to LKR 180.60 from LKR 172.95 in 2016. The Group ROE increased to 9.2% during the year from 7.6% in 2016 while Group ROA improved to 1.9% from 1.7% in the previous year.

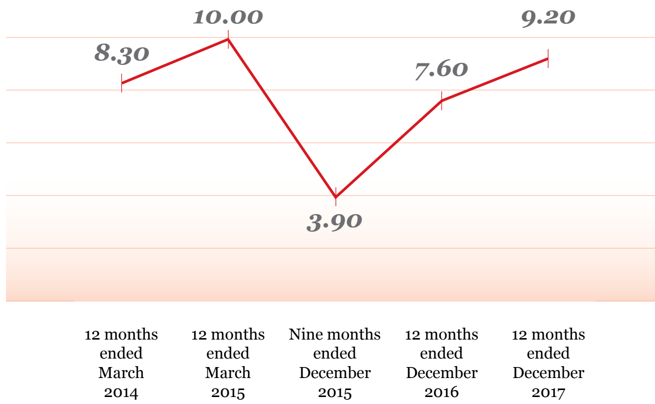
During the year, the compliance on minimum capital requirements changed from BASEL II to BASEL III with effect from 1 July 2017. This has brought up additional capital requirements through further stringent measures.

The requirement of BASEL III is phased out till 2019 commencing from Tier 1 and total capital ratios of 7.25% and 11.25% in the year 2017 to 8.50% and 12.50% in 2019 respectively. DFCC Bank achieved the current year requirements very comfortably by reporting 12.68% of Tier 1 and 16.13% of total capital as at December 2017. The Bank has planned its strategy to maintain healthy capital ratios within the next three years, in line with its business plan. Accordingly, the Board of Directors in January 2018, decided to issue LKR five to seven billion BASEL III compliant debentures subject to regulatory and other approvals to meet its future growth plans. This proposal was approved by the shareholders at the extra-ordinary general meeting held on 19 February 2018.

Return on Assets (Group) – (%)



Return on Equity (Group) – (%)



Credit Quality

During the year, the Bank was successful in growing its loan book covering corporate, retail and small and medium-term business segments. The expansion into new geographical areas and new customer segments increased the challenge to maintain a sustainable risk profile. The Bank improved its pre and post credit monitoring mechanisms through changes to internal processes and timely actions. This has brought positive results to improve credit quality. The Bank's non-performing advances ratio (NPA ratio) improved to 2.77% from 2.97%. Provision cover on impaired loans computed as per accounting standard LKAS 39 improved to 78.1% from 77.2% in the previous year.

Dividend Policy

The Banking industry faced many challenges during the year; both from business and regulatory fronts. The adverse weather conditions and adverse economic conditions due to lower GDP environment that prevailed during the year became constraints for the growth of returns on equity. The minimum capital requirements became more stringent with the adoption of BASEL III. The full year impact of the 4% increase in Financial VAT rate (introduced in May 2016) was felt in the year 2017. In addition to the external factors, DFCC Bank is undergoing a growth stage consolidating its position as a fully-fledged commercial bank. The Board of Directors after considering all the above priorities has approved a dividend of LKR 5.00 per share for the year ended 31 December 2017.

Group Performance

The DFCC Group consists of DFCC Bank PLC and its subsidiaries; DFCC Consulting (Pvt) Limited, Lanka Industrial Estates Limited (LINDEL), Synapsys Limited, its joint venture company Acuity Partners (Pvt) Limited (Acuity) and its associate company National Asset Management Limited (NAMAL). LINDEL is a 31 March reporting entity while others are 31 December reporting entities. For the purpose of consolidated financials, 12 months results from 1 January to 31 December 2017 were accounted in all Group entities. Financials of 31 March entity was subject to a review by its External Auditor covering the period reported.

The Group made a profit after tax of LKR 4,434 million during the year ended 31 December 2017. This is compared to LKR 3,469 million made in the year 2016. DFCC Bank accounted for majority of the Group profit with profit after tax of LKR 4,415 million while LINDEL (LKR 146.1 million), Acuity (LKR 175.6 million) and DFCC Consulting (LKR 1.7 million) contributed positively by way of profit after tax to the Group. In the previous year, share of profit from Acuity and LINDEL reported profit after tax of LKR 149.4 million and LKR 110.7 million respectively, while DFCC Consulting made a loss of LKR 1.4 million. Synapsys, the financial technology arm of the Group reduced its loss after tax to LKR 12.5 million during the year from LKR 19.6 million in 2016. The associate company, NAMAL contributed LKR 9.4 million to the Group down from LKR 11.8 million in the year 2016. An Inter-company dividend of LKR 91.4 million was paid to DFCC Bank by LINDEL (LKR 51.4 million), NAMAL (LKR 6.8 million) and Acuity (LKR 33.2 million) during the year.

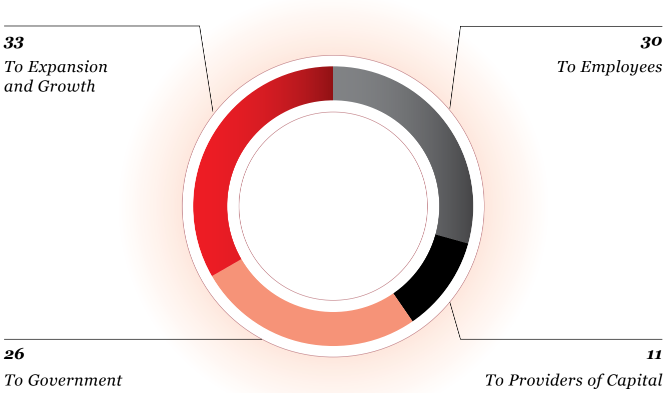
Value Added Statement – Bank

	For the year ended 31 December 2017			For the year ended 31 December 2016		
	LKR million	**LKR million**	**%**	LKR million	LKR million	%
Value Added						
Gross income		**35,942**			26,754	
Cost of borrowing and support services		**(23,980)**			(17,277)	
Impairment for loans and other losses		**(1,176)**			(937)	
		10,787			8,540	
Value Allocated						
To employees						
Salaries, wages and other benefits		**3,167**	**30**		2,809	33
To providers of capital		**1,193**	**11**			
Dividends to shareholders					663	8
To Government						
Tax expense	**1,377**			1,125		
Value added tax and nation building tax on financial services	**1,459**	**2,836**	**26**	986	2,111	25
To expansion and growth						
Retained Income	**3,222**			2,626		
Depreciation	**369**	**3,591**	**33**	331	2,957	34
		10,787	**100**		8,540	100

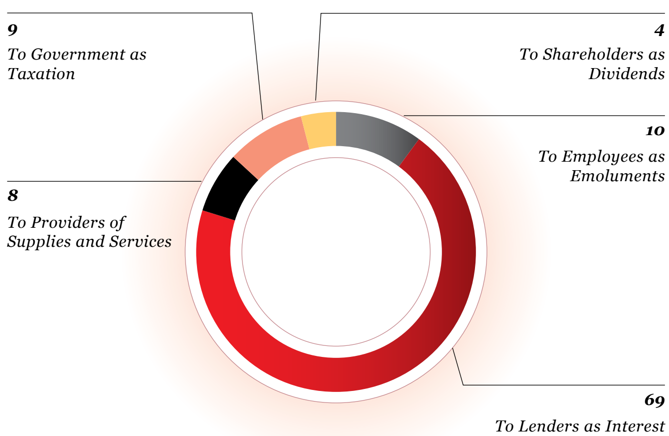
Sources and Distribution of Income – Bank

LKR million	**For the year ended 31 December**	For the year ended 31 December	For the nine months ended 31 December	For the year ended 31 March	
	2017	2016	2015	2015	2014
Sources of Income					
Interest income	**32,987**	24,194	8,918	8,010	9,530
Income from investments	**2,238**	1,165	641	2,150	1,211
Other	**717**	1,395	477	234	(260)
	35,942	26,754	10,036	10,394	10,481
Distribution of Income					
To employees as emoluments	**3,167**	2,809	1,248	943	906
To lenders as interest	**21,644**	15,294	5,560	4,675	4,894
To providers of supplies and services	**2,335**	1,983	913	587	576
To Government as taxation	**2,836**	2,111	864	1,116	1,056
To shareholders as dividends	**1,193**	663	1,591	1,458	1,325
Retained in the business					
Depreciation set aside	**369**	331	157	140	137
Provision for losses	**1,176**	937	225	(308)	324
Reserves	**3,222**	2,626	(522)	1,783	1,263
	35,942	26,754	10,036	10,394	10,481

Analysis of Value Addition (Bank) – %



Sources and Distribution of Income (Bank) – %



DFCC Bank's Business Unit Performance

Corporate Banking

Committed to environmental and social sustainability, the Bank continued to explore new avenues in financing renewable energy projects. In 2017, the Bank granted term loans to establish two waste-to-energy projects which will generate electricity using municipal solid waste collected within the Western Province. With each project generating 10MW, a total of 1,100 MT of municipal solid waste will be consumed per day, waste which would otherwise be dumped into landfills resulting in the creation of garbage mountains and leading to events such as the Meetotamulla tragedy which resulted in the loss of human lives in April 2017. The second 10 MW ground based solar power project at Hambantota financed by the Bank was commissioned during the year. Both these projects have posted impressive operating results.

The Ceylon Electricity Board offers competitive tariffs for small scale solar photovoltaic installations under the Net Plus and Net Accounting methods, providing a lucrative opportunity for owners of large rooftops to reduce their electricity costs and generate economic returns.

Recognising this, the Bank financed rooftop solar projects of 10 MW distributed across several factory buildings during the year, and anticipates providing financial support for many more projects.

Continuing a 2016 initiative to develop a sizable offshore lending portfolio focusing on emerging markets in South Asia and East Africa, the Bank granted a US Dollar term loan facility to part finance the construction cost of a 7.6 MW mini-hydro power project in Uganda with a majority holding by Sri Lankan investors. The Bank is also in the advanced stages of negotiations on two term loan facilities for hotel companies in Maldives. The Bank will continue to actively pursue further offshore lending opportunities in East Africa and South Asia.

Performance

The Corporate Banking department recorded a portfolio growth of 12.3% during 2017 despite the year presenting a challenging operating environment. While recording this growth, the department maintained its non-performing ratio at nearly 0%. This was a testament to the prudential measures adopted in granting credit and the stringent continuous monitoring of credit facilities granted.

Future Outlook

Focus was placed on improving fee-based and transactional income to the Bank in 2017. With a state-of-the-art “Payments and Cash Management” (PCM) solution recently launched by the Bank, 2018 will see more focus on the promotion of this solution to corporate clientele, which will improve the Bank’s CASA position and fee-based income opportunities.

With customers being a core focus of the Bank, the Corporate Banking Department held several customer-centric events during the year to improve fellowship with customers, identifying their needs to better align the Bank’s products and services to the aspirations of customers.

Business Banking

Positioned in-between Branch Banking and Corporate Banking, DFCC Bank’s Business Banking combines the best of both ends of the spectrum, offering an entire range of banking services, inclusive of commercial banking counter operations and lending products. The Bank maintains a close and cordial relationship with a diverse portfolio of clients, from lower-end corporate clients and higher-end SME clients, to retail customers.

Business Banking products include:

- Project loans
- Term loans for financing of business assets and construction of commercial buildings
- Loans and overdrafts to finance working capital
- Trade finance to facilitate imports/exports
- Debenture investments
- Fee-based products such as Letters of Credit and guarantees to cover transaction-related contingencies
- Personal financial services such as credit cards, leasing, personal loans, and housing loans.

Performance

During the period under review, the Business Banking assets portfolio grew by 20.4% to LKR 26,232 million – an impressive achievement. The loan portfolio contributed significantly to the growth of the asset portfolio.

Furthermore, the Business Banking deposit base, consisting primarily of fixed deposits, grew by LKR 2,592 million. The aggregate liability base stood at LKR 13,511 million as at 31 December 2017.

The Consumer Banking Assets portfolio grew by 21.2% to LKR 1,223 million. The Business Banking Unit was the largest contributor to the overall growth of the Consumer Banking Asset portfolio of the Bank.

Future Outlook

The Business Banking Department will focus on growing the CASA base in 2018 by adopting a strategy of developing new relationships while strengthening the existing relationships.

Branch Banking

EIB SME and Green Energy Global Loan

DFCC Bank implemented the EIB SME and Green Energy Global Loan credit line in March 2014. 70% of the credit lines was allocated for SME projects and the balance 30% for renewable energy and energy efficiency projects.

The entire loan of EUR 90 million was allocated within the stipulated period. This amounted to approximately LKR 14,478 million for 171 projects (net of cancellations) from three participating intermediary banks, including DFCC Bank. During 2017, supplementary allocations were granted to existing beneficiaries to finance cost overruns and expansions of approved projects with a view of utilising additional funds made available due to prepayments and gains from foreign exchange fluctuations.

During 2017, LKR 2,128 billion was disbursed as refinance to intermediary banks for the benefits of their customers. LKR 14,533 million has been disbursed in total.

SME projects in a variety of sectors including auto services and repair, bakery products, construction, education, healthcare, manufacturing including agro-processing, printing, retailing, tourism, and trading have been funded by this credit line.

Furthermore, a total of 18 renewable energy-based power generation projects with 56.7 MW of total planned capacity *via* solar, wind, bio-mass, and mini-hydro technologies were financed by the credit line. By year end, a total of 16 projects with a capacity of 53.7 MW were operational.

34.2%
***Profit Growth** (Bank)*

2.77%
***NPL** (Bank)*

14.8%
***Asset Growth** (Bank)*

34.3%
***Income Growth** (Bank)*

16.13%
***Total Capital Ratio** (Bank)*

Commercial Lending

The Bank's six decades of experience in development financing contributed positively towards increasing the project loan portfolio in 2017. Branch Banking actively participated in many concessionary loan schemes including EIB, SMILE III (RF), SMELoC, *Saubhagya*, *Jaya Isuru*, and *Ran Aswenna*. Loans and leases worth over LKR 3,800 million were granted through concessionary loan schemes covering key development sectors in Sri Lanka during the year. Active efforts will be taken to promote the Environmental Friendly Solution Fund II (E-friends II) revolving loan scheme that was established during the latter part of 2017 through the branch network to facilitate enterprises to comply with environmental standards and encourage pollution control and resource recovery initiatives.

Performance

Branch Banking recorded an overall asset growth of 15% in 2017, with 17% of growth in commercial lending.

In the face of stiff competition, Branch Banking was able to increase the overall liability portfolio by 35% while maintaining the CASA at 25%.

The credit portfolio remained healthy, in spite of the slow growth in the economy and natural disasters experienced during the year. This was the result of the Branch Banking Unit taking a proactive stance towards follow-up and recovery procedures adopted during the year.

Future Outlook

The primary focus in 2018 will be on increasing the customer base of the Bank, with a particular focus on retail clients that will pave the way to grow the CASA and retail lending portfolios.

Facility processing and recovery will be improved in regional offices and central units, which will aid branch teams in becoming more customer-centric.

To ensure continuous improvement of the Bank's retail portfolio, a Central Collection Unit will be established to drive delinquency management and early collections.

Personal Financial Services/ Consumer Banking

The Consumer Banking Unit aims to provide seamless banking solutions for the individual client. An individual can avail an entire range of flexible financial solutions catering to their needs, including personal loans, housing loans to purchase, build, or buy one's own home or apartment, vehicle loans and leasing, and educational loans and advances.

Consumer Banking also offers a host of attractive deposit products catering to the entire family, from newborn to senior citizen. Individual customers can benefit from the DFCC Virtual Wallet, a revolutionary breakthrough in digital payments that offers retail customers a hassle-free and convenient option to manage their funds eliminating the need to carry other payment instruments.

Liabilities

Consumer Banking CASA saw a major push in 2017, with the desired results achieved through branch expansion and new initiatives rolled out throughout the year. Aggressive campaigns aimed at instilling the habit of saving as a family unit were carried out across the branch network. Starting in January, a family savings campaign was launched, rewarding entire families that saved together. Families were rewarded with exciting gifts in April for the New Year and at the end of the year, in keeping with the spirit of the season. The drive to increase the number of accounts culminated in a marked improvement, achieving 200% year-on-year growth, primarily through branches out of Colombo.

"Vardhana Junior", the Bank's savings product for minors, was re-launched in July 2017 with an array of exciting gifts for children. Campaigns were carried out at schools, hospitals, and other locations across the island to raise awareness of the product. The product recorded a growth of 28% for the year, exceeding targets.

DFCC Bank continued to offer various savings products around the year, coupled with attractive interest rates and rewards on products such as Xtreme Saver, Mega Bonus, and Supreme *Vaasi*. The Xtreme Saver product emerged the star performer.

Performance

Consumer Banking liabilities grew by 30%, marking an excellent year. Time deposits grew by 36% and CASA grew by 12%, the two largest contributors to liability growth.

The overall liability performance was well above target, with the majority of growth experienced in Colombo and its suburbs, the Southern Central and North Central regions also recorded strong growth.

Future Outlook

DFCC will continue its efforts to grow the CASA in 2018, with several developments in the works, innovations backed by cutting-edge technology and investments in new channels of delivery apart from brick and mortar. Although catering to the future generation will be a challenging task, the Bank is fully geared to face the future head on, offering a breadth of seamless banking solutions that give customers unmatched value and unique benefits.

Consumer Assets

DFCC Consumer Assets is a relatively new entrant into the arena taking off in 2016 with DFCC Bank positioning itself as a fully-fledged commercial bank. 2017 witnessed a steady growth with the portfolio recording a 10% growth closing at LKR 35,000 million.

Much emphasis is placed on the growth of the Bank's retail portfolio considering the challenges faced in the industry with diminishing margins on interest. Furthermore, retail banking also plays a predominant role in contributing to the CASA growth of the Bank. 2017 witnessed an aggressive drive in obtaining employee pay roles while extending flexible and competitive employee banking solutions.

During the year 2017, new developments in products and processes took place, offering the individual customer a host of innovative offerings. In a bid to attract fixed income earners, employee banking solutions were actively marketed across the branch network. The increase in reach brought in new opportunities and many campaigns targeting specific segments were carried out which contributed to achieving the desired outcome. DFCC Bank's team of dedicated Business Development Officers continued to serve customers at their doorstep thereby ensuring that they received the very best of service.

Performance

On analysing the retail lending portfolio, 74% of the base attributes to regions out of Colombo. The year 2017 also witnessed majority of the growth taking place out of Colombo.

Future Outlook

Consumer assets will continue to play a key role in 2018. A continued investment in technology will result in a dynamic and innovative digital strategy across operations, driving the Bank towards an era of online applications, transactions, and processing. Value addition and customer care will be the focus of further investment going forward, with the Bank focused on adding broader and more diversified products. The Bank will continue to expand the branch network and increase its brand presence, particularly in key rural areas and up-and-coming towns across the country with potential for growth in consumer banking.

Housing

Marketed as part of the total Consumer Banking Solution, our housing product targets a wide cross-section of demographic comprising executives, professionals, private and public sector employees, and entrepreneurs. Growth was significant in fast developing urban areas and regions out of Colombo, due to the expansion of the branch network. Target growth was enabled through a number of campaigns aimed at specific segments.

The surge in high-rise buildings in the skyline of Colombo has opened up many opportunities for home loans, for the Bank to capitalise on – it entered into tripartite agreements with a number of reputed developers. The loan book saw significant contributions as a result of the Bank successfully catering to the high net-worth and middle income segments in apartment financing. Dual citizens and citizens employed abroad also benefited from the housing loans. Borrowers were offered complementary fire insurance policies on housing loans, in addition to attractive pricing.

Performance

The housing loan portfolio recorded a substantial growth of 20% in 2017. Offering a tailor-made product to build, buy, renovate, or improve one's home, *Sandella* Housing loans also covers the purchase of land and condominiums.

Leasing

A pioneer in the Leasing industry, DFCC boasts of a proud heritage of contributing to the development of the nation. Since 1984, DFCC Leasing has provided leasing solutions that cater to both SMEs and individuals.

DFCC Bank continued to offer machinery leasing, contributing to the growth of the SME sector. To cater to demand for commercial vehicle leasing, the Bank entered into strategic tie-ups with leading brands such as Tata from DIMO, Fuso and Mitsubishi from United Motors during the year. Apart from competitive interest rates, the Bank's team of Business Development Officers continues to service customers at their doorstep.

Performance

2017 proved to be a challenging year for leasing, with the Government having mandated tighter loan-to-value ratios and other regulatory measures. Despite the tougher climate, the leasing book recorded a growth of 4% with substantial disbursements. Growth was spurred primarily from Western province, with equally strong growth in the North Western and Southern regions.

Personal Loans

Personal loan products were used as a tool in a pull strategy to stimulate growth of the Bank's salary account base and Employee Banking solutions. Packages were crafted to suit various fixed income segments and a cross section of demographics covering lower, middle, upper middle, and high income categories in private and Government service.

The year saw the launch of a new product, "Vardhana Double Winner", offering a personal loan coupled with an overdraft to provide customers with access to credit in case of an emergency.

Performance

Competitive pricing and process improvements resulted in the product growing by 13%.

Future Outlook

Personal loans will be used increasingly going forward to grow the Bank's CASA base, with a primary focus on fixed income earners.

Gold-pledged Lending

Pawning products continued to grow during the year, as it proved to be an easily accessible and convenient source of emergency funding.

Performance

Strong demand for the product was recorded mainly out of Colombo, with substantial growth in the North.

Future Outlook

Coupled with a high advance value and an excellent service, the growth momentum is expected to continue into 2018.

Card Operations

The DFCC Bank credit and debit cards offer customers access to over 37 million merchants worldwide and accessibility to over three million ATMs worldwide.

Having obtained principle membership status with Visa International in 2016, the Bank continued to invest in the card business in 2017. A new credit card management system was implemented in November 2017, the first of its kind to be developed locally on a par with the highest international standards, as approved by Visa International. With the implementation of the new system, the Bank has setup the business model for cards to grow in 2018.

DFCC credit card holders were offered attractive discounts at leading merchant stores during the Christmas season. Users continue to enjoy discounts around the year and value added services, such as "loan oncard" which allows customers to obtain cash up to 75% of their credit limit, and a balance transfer facility with the lowest rates in the market. Flexi plans offer customers more convenient ways to better manage their finances for purchases over LKR 10,000 and the flexibility to repay via up to 24 month installment plans.

In line with its customer focus, DFCC Bank established connectivity with the common ATM switch through LankaPay, allowing DFCC customers to access their account through over 3,600 ATMs locally. Common Electronic Fund Transfers (CEFT) were also enabled for credit card payments in January 2018.

The Bank also offers customers the Multi Currency Global Travel card in its product portfolio, a prepaid card which enables pre-loading and access to four international currencies in one card at any given time. The product can help customers to significantly reduce the costs that arise from multiple currency conversions.

With the assistance of a global processor since the third quarter of 2015, the Bank provided a credit card acceptance technology to merchants. As at the end of 2017, over 300 merchant establishments have been equipped with the card acceptance technology.

Performance

During 2017, the Bank reported a total of over 148,000 debit cards with 35,000 new cards being issued. Debit card usage stood at LKR 4,600 million, representing 126,000 ATM transactions, and LKR 830 million from 325,000 POS terminal transactions.

The aggregate credit exposure of the credit card portfolio stood at LKR 880 million as at 31 December 2017, representing a card usage of LKR 485 million.
Despite the Bank's late entry into the market, the credit cards operations remain a viable business line. The prudent screening methods employed by the Bank in the issuance of credit cards has kept the card portfolio free of material mismatches.

Future Outlook

The Bank will continue to invest in the growth of the cards business and aims to launch new credit card products in 2018. EMV chip technology for debit cards and contactless credit cards are to be introduced in 2018 to provide enhanced security and ease of access for DFCC cardholders.

Premier Banking

DFCC Bank commenced Premier Banking operations in 2012, aimed at clients who maintain deposits or advances of over LKR five million or an equivalent amount in foreign currency. In addition to providing a speedy and reliable service that the Bank provides to all its clients, this elite membership is offered a wide array of products and services.

The Premier Banking clientele comprises of high net-worth individuals based both in Sri Lanka and abroad. The knowledge and expertise of the entire group is leveraged towards maximising the return on investments, while adhering to the risk appetite of the diverse range of clients. Understanding the busy lifestyle of premier clients and their demand for a superior level of service, a dedicated Relationship Manager is assigned to serve each of them.

Continuing to stay ahead of the competition and leverage on information technology in pursuit of developing the Bank's relationship with its clients, the Bank launched the "Premier Go" app, an industry first. Through this app, clients can connect with their dedicated Relationship Managers anywhere in the world, be updated on current promotions and offers, view account balances, schedule appointments, and keep track of their finances.

The revamp of the Premier proposition saw the Margin Trading product being revived with changes made to the marginable stocks and relaunched to suit the needs of equity investors. The product was demonstrated amongst the stockbroking community at a stockbroker function held to promote the product. Premier clients were offered complimentary invites and tickets for exclusive events around the year, such as the Annual Sri Lanka Directors' Dinner organised by the Sri Lanka Institute of Directors, and stage plays of veteran playwright-cum-actors. DFCC Bank was also proud to sponsor the Inter School Golf Tournament hosted by the Royal Colombo Golf Club in 2017.

Performance

The premier customer base increased by 45%, which led to a deposit growth of 45% and advances growth of 80% on a year-on-year basis in 2017.

Institutional Business and Product Development Unit

Formed in January 2017, the objective of the Institutional Business and Product Development Unit is to drive business among institutional clients (non-individual) and carry out product development initiatives across the Bank in a focused and structured manner. The Unit's work scope is built under the following pillars:

(a) Institutional deposits

(b) Trade business

(c) Product development

Institutional Deposits

Due to DFCC's strength traditionally being in lending, the Unit had a challenge to lead a shift in mindset across the Bank to move towards deposits. To achieve this objective, a series of both internally and externally focused strategies and projects were planned and rolled out around the year.

Performance

This resulted in the Bank growing its overall institutional deposits to LKR 34,336 million as of 31 December 2017 from LKR 23,859 million as of 31 December 2016, an unprecedented year-on-year growth of 44%. The high importance given to CASA mobilisation enabled institutional CASA deposits to grow by LKR 1,627 million during the year, to LKR 8,256 million as at 31 December 2017 from LKR 6,629 million as of 31 December 2016. An institutional CASA ratio of 24% was achieved as of 31 December 2017.

Trade Business

The Institutional Business Unit was tasked with driving Branch Banking trade business and contributing towards boosting trade fees and commission income. Through the identification of critical success factors, a multi-dimensional business model was developed and a series of carefully planned initiatives rolled out with clear timelines under central supervision. A team was handpicked to execute the strategies at ground level and provided with technical training and business skill coaching. Effective mechanisms for close central monitoring and follow-up were introduced to ensure delivery of action plans.

Performance

As a result of the integrated approach, Branch Banking import limits achieved a growth of over 52% within a time period of approximately six months while achieving extremely high levels of utilisation. Healthy growth in export limits was also seen while utilisation remained consistently high. Large scale personal visit campaigns aimed at key trade client segments helped in penetrating previously untapped segments.

Product Development

Set up in January 2017, the objective of the Product Development (PD) Unit is to ensure the Bank offers attractive and unique products to suit the constantly changing market. It does so by taking responsibility for bringing multiple internal stakeholders together as part of the product development exercise at any stage, be it idea initiation, development, execution, or analysis. In its first year, the Unit was able to launch and revamp several products and campaigns, while complying with the Bank's Product Development Policy.

A successful CASA building campaign, the *Avurudu* hat-trick, was carried out in April. A follow-up campaign was carried out in October, in view of the Thrift Month.

"Vardhana Junior" a savings product for minors, was relaunched in July and stood out from competitor offerings as the most attractive savings product for minors. The relaunched product offered attractive gifts and introduced a unique rewards scheme aimed at Grade 5 scholarship students.

In partnership with WebXpay, a new product proposition was launched to offer mutual business clients unique cost-effective m-Commerce solutions and financial services to enable them to launch and carry out their businesses online.

Supporting the Bank's vision of achieving one million customers by 2020, an internal campaign, "Road to a Million Customers", was launched between October and December 2017, helping to increase the client base significantly, encouraging staff members to serve as proud brand ambassadors for DFCC.

As part of its efforts to strengthen the Bank's CASA products with additional features, PD introduced Life and Hospitalisation Covers for customers who saved with DFCC during the festive season. The Unit will continue this momentum by introducing many more unique offerings to the market, ensuring that the Bank and its customers will "Keep Growing".

Treasury

The Treasury Front Office (TFO) of DFCC Bank consists of three main income generating units: the Foreign Exchange and Money Markets Unit, the Fixed Income Unit, and the Treasury Sales Unit that report directly to the Head of Treasury.

The Treasury Middle Office (TMO), functioning independently under the purview of the Chief Risk Officer (CRO) monitors the risks assumed by the Front Office based on Board-approved limits and controls. TMO operations were further enhanced during the period under review in line with the regulatory guidelines.

The Treasury Back Office (TBO) is accountable for the preparation, verification, authorisation, and settlement of all transactions made by the TFO. The TBO independently reports to the Head of Finance/Chief Financial Officer, in compliance with regulatory guidelines.

During the period under review, the Standard Deposit Facility (SDF) and Standard Lending Facility (SLF) rates of the Central Bank of Sri Lanka (CBSL) were revised upwardly by 25 bp to end the year at 7.25% and 8.75% respectively. This is in line with the tightening cycle adopted by the regulator since the end of 2015. No further upward revisions to the rates are expected during the first half of 2018.

The country's economic achievements have been recognised by rating agencies Fitch and Standard & Poor, where both upgraded the country's outlook to "stable" from "negative". The rating agencies anticipate the Government will maintain the reform momentum over the next 12 months and manage the debt redemptions efficiently.

The US Federal Reserve raised their target rate thrice in 2017, leaving the rate at a range of 1.25% to 1.50%.

With surplus liquidity in the market during the second half of the year, the interbank money market rates (overnight rates) continued to slide to close the year at 8.15%, compared to 8.42% at the start of the year. Closing market liquidity was around LKR 9,700 million. Risk-free Treasury Bill and Bond yields also followed suit, particularly during the second half of the year. It is noted that the one year Treasury Bill rates stood at 8.90% compared to 10.22%, while five year and ten year Bonds reduced to 9.60% from 11.90% and to 11.00% from 12.50% by the end of the year.

The Dollar-Rupee market was fairly stable during the year due to the CBSL allowing market forces to seek its equilibrium. The YTD depreciation in LKR has been limited to 2.35% in the backdrop of strong inflows to the equity and bond markets, particularly since the second quarter of the year. Improved foreign investor appetite in the region and domestic developments added to the positive momentum. The country witnessed foreign inflows to the debt and equity markets of LKR 64,178 million and LKR 17,654 million respectively. Stability in the currency markets was boosted by the successful completion of Sovereign Bond issuance by the Government of Sri Lanka in May 2017 where the Government successfully raised USD 1.5 billion through a ten year sovereign bond with a final order book exceeding USD 11.5 billion. This resulted in higher foreign exchange (FX) reserves.

The IMF standby facility helped to add confidence to investors seeking economic stability as a precursor for investing in the country. Improved export earnings partly contributed to the regained GSP+ benefits, and a robust tourism sector are other factors that contributed to increased confidence in the country. The commendable performances in these sectors have managed to offset the negative impact of declining worker remittances to the country.

The less volatile and predictable currency movement in LKR has helped the banks to better manage their foreign exchange risk while quoting the customers very attractive exchange rates on their transactions as a result of the reduction of the risk premiums. This would also help to improve appetite of the foreign investors of the country as they can now project the future returns more accurately.

Performance

The Treasury Fixed Income (FI) desk made major gains during the year through trading activities while contributing considerable interest income to the bottom line. Given the lack of opportunities in the market, these are significant achievements. The FI portfolio stood at LKR 55,990 million while the encumbered portfolio (reserved for repurchase agreement transactions) stood at LKR 5,640 million at the end of the year.

DFCC Bank's Treasury recorded LKR 270.39 million through FX trading activities while also reducing the cost of funds through its FX swap operation.

Future Outlook

With customer service in mind, the Treasury will move forward to engage in a series of process improvements with the support of the IT department. With the focus being on upgrading the existing treasury system to a new system, the department will be able to handle the increasing workload while improving overall efficiency.

Resource Mobilisation Unit

The Resource Mobilisation Unit falls under the direct purview of the Head of Treasury. It manages all term funding of the Bank, including *inter alia*, credit lines, syndicated loans and local and international debt issuance. The Unit coordinates with rating agencies in their reviews and works to secure ratings for debt issuances. The Unit also manages the Bank's equity and Unit Trust portfolios, related strategic and non-strategic investments and divestments.

DFCC Bank's Investment Portfolio

As at 31 December 2017, the combined cost of investments in DFCC Bank's holdings of quoted shares [excluding the investment in the voting shares of Commercial Bank of Ceylon (CBC) PLC], unquoted shares, and unit holdings amounted to LKR 1,470.61 million.

The composition of the investment portfolio is detailed as follows:

Investment Portfolio as at 31 December 2017

	Cost (LKR million)	Market value (LKR million)
Quoted share portfolio (excluding CBC voting)	715.48	928.72
Unit trust portfolio	669.58	838.95
Unquoted share portfolio	85.55	85.55
Total	**1,470.61**	**1,853.22**

The cost of the unquoted share portfolio is carried at cost on the balance sheet. The market value of the holding in the voting shares in CBC was LKR 17,262.50 million as at the end of December 2017, against a cost of LKR 4,866.53 million. During the year, the Bank made an investment of LKR 1,413.82 million in CBC rights issue to purchase the rights entitlement and made an additional LKR 113.6 million investment to purchase one million additional rights. During the same period, the Bank divested 10.79 million shares of Commercial Bank and realised of LKR 1,091.50 million as capital gains.

Additionally, the Bank divested a part of other quoted, unquoted shares, investments in unit trusts and realised LKR 77.33 million as capital gains. During the period under review, the Bank also made new investments in quoted shares to the value of LKR 17.85 million.

Bancassurance

Since its inception in mid-2014, Bancassurance operations have continued to grow. The life insurance business in particular has experienced significant growth since its streamlining exercise conducted at the end of 2016, with the signing of a long-term agreement with AIA Insurance Lanka PLC. The result is a dynamic product and service offering for the Bank's customer base.

Loan and lease customers benefited from insurance advisory, rates, and claim settlements through the Centralised General Insurance Operation, part of the DFCC Bancassurance operation.

The Bancassurance Unit hosted many events and programmes around the year to raise customer awareness about the mitigation of risks associated with business and life. Customers were educated about financial planning and retirement planning, and received advice on planning for their children's higher education needs.

Performance

The Bancassurance business made a noteworthy contribution to the Bank's bottom line, with high potential for future growth.

Future Outlook

Protecting its customer base from all possible risks objective associated in business and life is the underlying motive of DFCC's Bancassurance business. To that end, the Bank continues to work to introduce new products adhering to international standards and quality.

International Banking

Trade Services

Sri Lanka's exports hit a record USD 11.36 million in 2017, a 10% growth over 2016. Imports grew by USD 18,931 million, a growth of 9% over 2016.

After the Budget proposal in the last quarter of 2017, the Bank experienced a substantial increase in the issuance of Letters of Credit related to vehicle imports.

Over the course of the year, the Bank was able to take on new trade clients via the branch network and the coordination between the Business Banking and Corporate Banking units. The Bank established a separate trade unit at the Pettah Main Street branch to improve the speed and quality of its service to its trade clients.

Through the improvement of processes to cater to customer requirements, the expansion of the correspondent banking network, along with a dedicated and knowledgeable trade team, the Bank was able to grow its trade client base and improve repeat business in 2017.

Performance

The Bank's import and export volumes in 2017 grew 13.1% over the previous year.

During the year, the interest income earned from import and export loans increased to LKR 2,469 million from LKR 1,728 million while fee and commission income increased to LKR 399.9 million from LKR 378.04 million.

Payments and Settlements

As part of the Bank's endeavour to rationalise operational processes, a dedicated unit for Payments and Settlements was set up at the outset of 2017. This department caters to the Bank's customer base island-wide, and handles remittances for foreign currency payments and receipts, and Domestic Payment Services (DPS) for Rupee transactions.

Domestic Payments Services is responsible for the Customers Cheque Clearing, Sri Lanka Inter-Bank Payment Systems (SLIPS), and Common Electronic Fund Transfer Switch (CEFTS) payments of the Bank.

The Remittances Department is accountable for Inward and Outward Telegraphic Transfers, Demand Draft Issuance and Collections, and is also responsible for all bill settlements of the Trade Services Division.

This specialisation approach has encouraged the staff to work together as a dedicated unit, ensuring accuracy and undertaking many precautionary measures to ensure the safety of the Bank's customers foreign currency payments, which can be susceptible to cyber crime.

Future Outlook

Even though many sophisticated electronic funds transfer mechanisms are in place now, the Bank experienced an approximate volume increase of around 5% in the cheque clearing process during 2017. In recognition of this, the Bank will be introducing a more efficient cheque clearing system during the first quarter of 2018, enhancing service standards in the Domestic Payments sphere.

The increase in business volumes during the year were not up to expectations. In 2018, the team is determined to drive towards budgets with the help of the branches, while capitalising on the ease of doing business with the introduction of the new Foreign Currency Act.

INSTITUTIONAL CAPITAL

Organisational Knowledge

The Bank recognises the value of sharing knowledge across the organisation, as it enables staff to solve problems more effectively, evolve to meet changing business requirements, and survive disruptive changes.

Management and dissemination of knowledge is enabled through provision of focused and customised training programmes relevant to employees job scope. These include knowledge sharing programmes by experts and technical and soft skill modules formulated with inputs obtained from cross-functional representatives. The Bank also operates an e-learning platform consisting of a range of technical and soft skills learning materials which is also a very useful tool to retain and disseminate knowledge. An intranet is also available to transmit corporate information to staff.

Systems, Processes and ICT

Continuing its digital journey in 2017, the Bank focused on providing multiple product options to various customer segments while enhancing the customer experience via digital channels.

Some of the key highlights in 2017;

- Supporting its corporate customer base, the Bank launched its own Payment and Cash Management (PCM) system. The system enables corporate customers to have complete control over their cash flows, including payments, collections, and liquidity management. Corporate customers can simplify their payment and collection processes by bringing their suppliers and customers into the PCM system.
- The Bank launched its own Card Management system with connectivity to the VISA network. The system increases the Bank's capacity to offer a full spectrum of services to its Credit and Debit card base.
- The Bank joined the Common Electronic Fund Transfer (CEFT) system, enabling online inter bank transfers over the counter and through online banking platforms.
- The Bank implemented an Enterprise Alert Platform, integrating all transaction-based systems and enabling the Bank to alert transaction parties of ongoing transactions, providing customers with virtually real-time notifications via SMS and email.

Payment and Cash Management

system simplifies Corporate, Business Banking and SME customers' payment and collection process

Electronic Fund Transfer system

enables online inter-bank transfers over the counter and via online banking platforms for our customers

Premier Go

app connects Premier customers directly to their dedicated Relationship Manager via video call

- As part of its commitment to the Green Bank Initiative and to enhancing customer experience, the Bank implemented an Electronic Statement System. Electronic statements enable the Bank to provide increased value addition to customers through detailed analysis of their spending and income patterns. Customers are offered the option of opting for a consolidated electronic statement instead of paper statements at no cost. The Bank expects to cut down approximately 50% of the paper used for printing statements.
- The Bank introduced a mobile app, "Premier Go", aimed at strengthening the relationship between the Bank and its premier customers. Besides providing account related information, premier customers can also directly communicate with their dedicated relationship managers over video via the app.
- The Bank's planning and budgeting system was completely migrated to Oracle Cloud, using the Software as a Service (SaaS) model, as part of its Cloud adoption strategy.
- New account opening was automated on a workflow platform, enhancing staff productivity and minimising processing lead times. The system is anticipated to reduce processing time by over 90%, and more process automation is planned for 2018.
- A new mobile app "Sales Talk" was introduced to empower the Bank's sales team, providing them with up-to-date information accessible from anywhere.

Corporate Culture and Values

The Bank is focused on building and nurturing a culture of appreciation, accountability and empowerment within an environment that promotes a relaxed atmosphere and encourages creativity and open communication.

Since the introduction of the Bank's revamped values in late 2015, a number of initiatives have been introduced to keep its core value system at the forefront of the minds of employees. Those who demonstrate behaviour reflective of the Bank's core values are recognised and rewarded and become a positive example to be emulated. In the latter part of 2017, the Bank introduced a new regional team challenge spanning six months which assigns a value for each region to champion and drive across the Bank. This encourages ownership as well as greater understanding and appreciation of these values.

DFCC Bank's ethos ensures that employees are encouraged to voice their opinions, views, concerns, and foster two-way communication. To this extent, the Bank held open days from time to time with the Chairman and CEO, providing staff with the opportunity to have one-on-one interactions with them. The "Reach Out" programme for female staff and the Grievance Committee further enable employees to raise concerns while the ongoing HR business partner programme is targeted towards enabling improved access to HR services. Progress and news on the Bank events are disseminated across the network in a weekly newsletter, and community boards have been introduced at selected offices which are regularly updated to keep employees abreast of the latest developments at the Bank.

DFCC Bank strongly believes that a workplace that proactively and frequently appreciates and recognises its employees is an environment that inspires employees to continuously strive to achieve more. The Bank has a number of schemes in place to recognise and appreciate employee contributions, such as the quarterly "Rewarding Excellence" scheme, where employees who go the extra mile are rewarded and recognised for their contribution. Through the staff appreciation scheme, departments and branches are provided an annual allowance for team celebrations. The Annual Awards Night is another event held to acknowledge and reward exceptional contribution by employees. In an effort to ensure improved team bonding, a host of different events are organised throughout the year which provide employees with avenues to interact socially while also engaging in activities of interest to them. Health and wellness continues to be a priority with many varied programmes offered throughout the year as well as employees being provided access to concessional gym and club memberships.

Brand Equity

DFCC Bank has a proud legacy extending over 60 years in Sri Lanka as the premier development financial institution in the country. The Bank is now a fully-fledged commercial bank. Providing a diverse range of financial solutions and products aimed at a range of customer segments, from retail and large corporates to Micro, Small and Medium Enterprises (MSMEs); DFCC Bank enables its customers to "Keep Growing".

The Bank is renowned for having nurtured entrepreneurs and start-up enterprises across all economic sectors since its inception in 1955. It continues to strengthen the relationships it has built with customers for decades, and work towards attracting newer customer segments by offering a range of financial solutions that suit their evolving needs.

Improving brand and product awareness in 2017;

- The Bank maintained its brand presence throughout the year, engaging in mass media communication, market activations, and revamping the appearance of bank branches. This resulted in attracting more customers to DFCC. The Bank continued to engage with customers through expanding the branch footprint and presence in multiple locations across the country.

- Raising awareness of the Bank's consumer banking and SME products and services was done through various means, including social and digital marketing, and increased brand visibility and product campaigns.
- The Bank built-up its brand association with sports through a tie-up with the Papare.com and sponsorships of sporting events. The Bank sponsored the Inter School Golf Tournament as the title sponsor, and the Gajaba Super Cross 2017 as the official banking partner. Additionally, the Bank also sponsored the Colombo International Tea Convention as the strategic partner.
- The Bank also initiated a special series of workshops, "Vardhana *Sahaya Hamuwa*", to nurture the growth of the Micro, Small and Medium Enterprises (MSMEs) in Sri Lanka. The primary focus of these programmes was to increase the financial literacy and financial management abilities of the MSME sector, in addition to promoting the Bank's financial services and products.

The Bank continues to strive to enhance its position among the top 25 brands in Sri Lanka. To maintain its brand equity, the Bank continuously monitors its brand performance. For instance, the Bank regularly carries out customer research to measure and enhance the quality of customer service across its branch network. The transformation to a fully-fledged commercial bank exposes the brand to an expanded customer base that demands increasingly customised solutions. In addition to staying relevant with the evolving needs of the identified customer segments, the Bank maintains a strong focus on sustainable growth of all its stakeholders, true to its positioning: Keep Growing.

Business Ethics and Integrity

The Corporate Governance Report on page 111 discusses the governing mechanisms DFCC Bank has established to uphold its business to the highest levels of ethics and integrity.

Anti-corruption

The Bank's Code of Conduct sets out detailed provisions in anti-corruption. These provisions have been thoroughly detailed to all Bank employees, and are supplemented through necessary updates.

DFCC Bank is a responsible corporate citizen, and ensures sustainability through maintaining its transparent and unblemished track record of business.

Compliance

DFCC Bank understands the importance of satisfying all laws, rules, and regulations that are imposed upon it as a financial services intermediary. The Bank's policies and procedures extend beyond default legal and regulatory requirements to incorporate wider benchmarks of integrity and ethical conduct. Measures taken to mitigate all compliance-related risks are laid out in detail under Operational Risk on page 101 of this Annual Report.

The Bank continues to maintain a faultless record, and has not been subject to any fines or actions implemented by regulators for the period under review for any instances of non-compliance. The Bank also continued to invest resources in training its personnel across all sectors in areas of regulatory compliance.

Value Creation and External Capital Formation

External capital is derived directly from our stakeholders; it is the value underpinning the diverse stakeholders of the Bank and the Group. The synergy between our internal and external capitals powers our business to deliver value to, and derive value from our stakeholders. Our commitment to the resilience of our relationships and profitability of our partnerships helps to increase the value we derive from our external capital in the years to come.

INVESTOR CAPITAL

Shareholder Profile

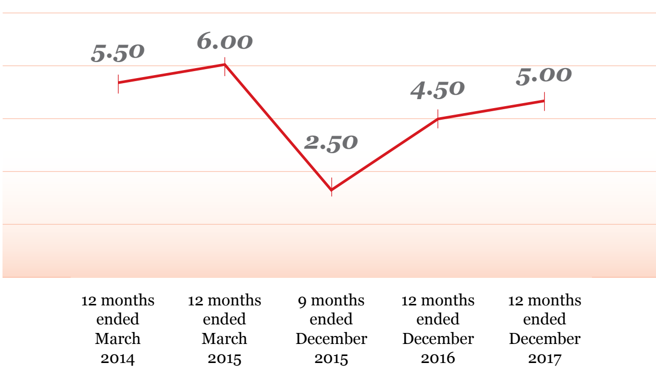
The Bank had 8,728 shareholders on 31 December 2017 (corresponding to a figure of 8,776 as at 31 December 2016), with the total number of shares in issue remaining fixed at 265,097,688 ordinary shares. Institutions account for approximately 84% of the Bank's share capital. 76% of the Bank's share capital is held by local shareholders, both institutional and individual. Similarly, local shareholders account for 98% of all shareholders.

Return to Shareholders – Bank

Description	2017	2016
Profit for the year (LKR million)	**4,415**	3,289
Return on total assets (%)*	**1.48**	1.30
Net assets per share (LKR)	**180.60**	172.95
Earnings per share (LKR)	**16.65**	12.41
Dividend per share (LKR)	**5.0**	4.5

** After eliminating fair value reserve*

Bank Dividends per Share – *LKR*



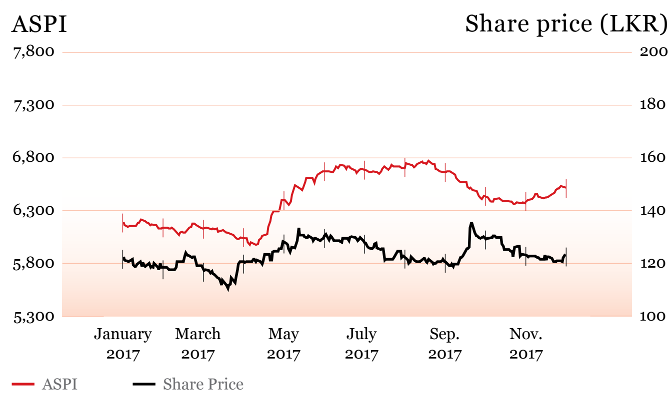
Financial Return

The Bank aims to regularly provide high total shareholder returns through profitable and sustainable performance.

The Directors approved a first and final dividend of LKR 5.00 per share for the year ended 31 December 2017. Dividends are based on growth in profits, while taking into account future cash requirements and the maintenance of prudent ratios.

Bank Share Price – *LKR*

Share Price Movement – *Jan. 2017 - Dec. 2017*



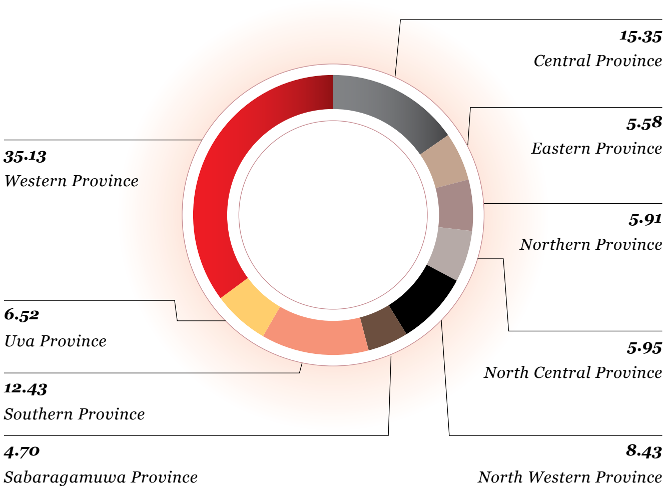
Refer page 144 for further details related to Investors.

CUSTOMER CAPITAL

Customer Profile

The expansion of the branch network was particularly concentrated in the Southern and Western provinces. The growth of the customer base in these provinces can be attributed to DFCC Bank's expansion in these areas, combined with promotional efforts and compelling products and services.

Customer Profile – %



Our Portfolio

Corporate Banking, Branch and SME Banking, Small Business Enterprise Banking, Business Banking, Consumer Banking, Premier Banking, Treasury, and International Banking are the Bank's primary lines of business. These business lines are complemented by the Bank's subsidiaries, a joint venture and an associate company for services in consultancy, industrial estate management, information technology, investment banking and fund management.

Through its growing island-wide branch network, the Bank offers a full range of development and commercial banking solutions.

35,000

new debit cards issued

Branch Banking recorded an overall asset growth of 15% in 2017, with 17% of growth in commercial lending

12.3%

Corporate Banking portfolio growth

20%

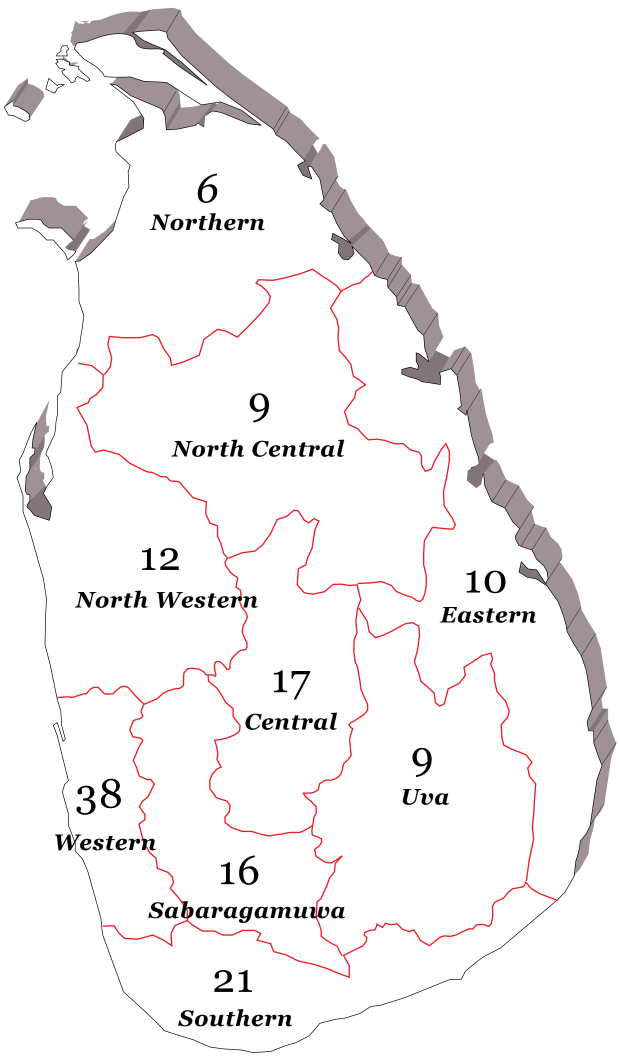
growth in housing loans

Product/Service	Target Segment
Project loans funded by credit lines *Saubhagya*	Small and Medium Enterprises (SMEs)
New Comprehensive Rural Credit Scheme	Short-term cultivation
Self-employment Promotion Initiative Loan Scheme	Vocational qualification holders
SMILE III Revolving Fund	SMEs
Commercial Scale Dairy Development Loan Scheme (CSDDLS)	Dairy sector
Small and Medium Sized Enterprises Line of Credit (SMELoC)	SMEs
Swashakthi (Micro and Small Enterprises Development Loan Scheme)	Micro and Small Enterprises
Loan Scheme for Resumption of Economic Activities affected by Disasters (READ)	For self-employed and small-scale businessmen to resume any economic activity affected by a disaster which has been recognised and informed by the Government of Sri Lanka (GOSL)
E-friends II Revolving Fund	SMEs
Jaya Isura	SMEs
Ran Aswenna	SMEs
Govi Nawodaya	SMEs
Rivi Bala Savi	Households that willing to purchase solar panels
Other project loans Term loans	Corporates, SMEs, professionals and individuals
Working capital financing → Short-term working capital financing – overdrafts, revolving credit or short-term working capital loans → Medium, long-term loans to finance permanent working capital requirements	Current account holders, corporates, SMEs, and entrepreneurs Corporates, SMEs and entrepreneurs
Vardhana *Sahaya* A one-stop financial solution offering loans, leases, bank guarantees and other commercial facilities for MSMEs	MSMEs
Leasing facilities "Easy Leasing" facilities for brand new and unregistered/ registered vehicles, machinery, plant and equipment	Corporates, SMEs, entrepreneurs, professionals and individuals
Hire purchase facilities Hire purchase facilities for vehicles	Corporates, SMEs, entrepreneurs, professionals and individuals
Guarantee facilities Bid bonds, advance payment bonds, performance bonds, bank guarantees for credit purchase of goods	Corporates, SMEs, entrepreneurs, professionals and individuals

Product/Service	Target Segment
Time deposits A wide range of tailor-made time deposit products at competitive interest rates	Corporates, SMEs and individuals
Loan syndication Loans provided by a group of lenders which is structured, arranged and administered by one or several banks	Corporates
Consultancy and advisory services Provision of legal, tax, finance, market and other advisory services to start up a new business or revamp existing businesses	Corporates, SMEs and entrepreneurs
Savings facilities Supreme *Vaasi* – Offers a superior rate of interest	Businesses and individuals aged 18 years and above
Mega Bonus – Interest rates grow in tandem with the savings deposits	Businesses and individuals aged 18 years and above
Xtreme Saver – Offers the highest interest rate for Rupee and Dollar denominated savings based on the account balance	Businesses and individuals aged 18 years and above
Vardhana Junior – Children's savings account offering a range of gifts and support for higher education	Children below 18 years of age
Vardhana Junior Plus – Children's savings account with a higher interest rate	Children below 18 years of age
Vardhana *Garusaru* – Offers an attractive interest rate with a range of other benefits	Senior citizens above 55 years of age
Personal loans Loans that help meet personal financing requirements	Self-employed individuals, professionals and salaried individuals
Salary Booster Overdraft facility that allows an advance of up to 90% of a month's salary	Salaried individuals
Pawning services *Ranwarama* Pawning – Gold-pledged advances	Mass market/individuals
Housing loans *Sandella* – Flexible and convenient housing loans at affordable rates	Self-employed individuals, professionals and salaried individuals
Education loans Vardhana *Nenasa* – Flexible and convenient loan facilities for higher education	Individuals pursuing higher studies
Other facilities Includes a range of products and services such as current accounts, overdraft facilities, foreign currency accounts, credit card facilities, DFCC Virtual Wallet, DFCC iconnect (Payment and Cash Management) gift certificates, international trade services, off-shore banking, international payments, Bancassurance, foreign money transfer via Western Union/Lanka Money Transfer and local payments.	Business community, entrepreneurs, professionals and individuals

Branch Network and Service Delivery

The Bank continued to expand its branch network in 2017, with a new branch in Western province, and 14 extension offices converted into fully-fledged branches. With the opening of a second branch in Pettah, the Bank grew its presence in a busy commercial centre with great business potential. Moreover, customers can access the Bank's services through 36 service points at Sri Lanka Post outlets and over 3,600 ATMs across the country. The Bank continues to use technology to expand its reach to customers beyond traditional brick and mortar, through Internet and mobile banking services.



Details of the branch network are given in the online report
http://dfcc2017.annualreports.lk/bn.html

Focus on Micro, Small and Medium Enterprises (MSME)

Established in 2016, the MSME unit addresses the financial needs of Small Business Enterprises (SBE) and has increased the Bank's penetration of the Small and Medium Enterprises (SME) sector. SBEs are enterprises positioned between SMEs and informal micro-enterprises. The Association of Development Financing Institutions in Asia and the Pacific (ADFIP) awarded DFCC Bank in May 2017 in the "SME Development" category for forming a specialised unit for the development of MSMEs.

The MSME unit offers "Vardhana *Sahaya*", a financial solution that provides loans, leases, bank guarantees, and other commercial facilities below LKR 3 million to SBEs involved in key sectors of the economy, including Agriculture, Livestock, Manufacturing, Services, and Trading. The Bank granted credit facilities to approximately 1,000 MSME customers in 2017 through Vardhana *Sahaya* and the *Swashakthi* Government funded credit scheme.

With the participation of key personnel from the Central Bank of Sri Lanka, the Bank commenced *"Sahaya Hamuwa"* in conjunction with the new product, a customer skill-enhancing programme series. Eight *"Sahaya Hamuwa"* programmes were conducted across many parts of the country, focusing on 'Entrepreneurship and Financial Literacy'. Aimed at entrepreneurs of SBEs, the programme provided an insight to entrepreneurship development, marketing, accounting, and record keeping.

New Product and Service Innovations

DFCC Virtual Wallet

The first of its kind in Sri Lanka's banking industry, the DFCC Virtual Wallet is an innovative mobile payment solution used by over 12,000 customers and over 1,100 merchants, a significant milestone.

The product has rapidly captivated both merchants and individuals, with increasing usage reported at both ends. The merchant base expanded into the E-commerce sector, and the Bank partnered with WebXpay to further strengthen its entry into the segment. The Bank also partnered with Aequm Lanka (Private) Limited to strengthen face-to-face transaction acceptance at small merchant locations.

Boosting the product's inherent convenience to customers, DFCC Chatz, an online chatbot, can be accessed via Facebook. The chatbot provides instant feedback on information relevant to the DFCC Virtual Wallet for both customers and merchants.

Customers were treated to exciting seasonal offers, with steep discounts at popular merchants, including online stores, clothing stores, restaurants, supermarkets, taxi services, and fresh seafood stores. Participating retailers were Tash, Laugfs supermarkets, Cotton Collection, Max Mara, Divine, Sandwich Factory, Kangaroo Cabs, Takas.lk, MyDeal.lk, OceansBestlk.com, and Direct2Door.lk. DFCC Virtual Wallet customers were afforded the opportunity to make use of this season's most generous discount offers.

The promotions conducted at business locations and other prominent marketing campaigns helped to successfully raise awareness of the product in the market and increase transactions routed through the application by new and existing users. The Bank is proud to spearhead this unique digital innovation that has helped to revolutionise payments and convenience to its customers, and will continue to encourage individual users and merchants to move away from the traditional use of physical cash.

Adding further value to the product in 2018 through promotions, campaigns and effective cross-selling, the Bank will continue to refine the product through new developments aimed at offering Sri Lankans liberal access to transacting via their mobile phones.

Lanka Money Transfer (LMT)

Lanka Money Transfer (LMT) is a state-of-the-art remittance system which enables instant remittances to accounts maintained at DFCC Bank PLC and any LMT Partner Bank/Financial Institution via a secure network. Migrant workers are able to quickly and securely remit their earnings through this service to their loved ones back home. Funds are credited to the beneficiary's account held at DFCC Bank or any other account held with LMT Partner Banks/Financial Institutions with minimal hassle. Adding to the convenience for customers, the Bank has ensured that it houses the best exchange companies under one roof.

Premier Go

DFCC Bank launched "Premier Go", the first premier banking app in the industry, exclusively for the Bank's premier customers in November 2017.

In addition to providing secure access to account and transaction information, the app empowers premier customers with direct access to their dedicated Relationship Manager via video conferencing.

Further details can be found on page 76, Industry Initiatives.

Product Responsibility

Transparency and clarity in product labelling is not only a responsibility of the Bank, but can also drive product sales. Consumers are increasingly tech-savvy and expect to be well-informed before committing to purchases and services. Social media and other online sources provide consumers with the means to broadcast their dissatisfaction to broad audiences, which can have negative impacts on the Bank's business and reputation.

DFCC Bank takes every effort to provide transparent and relevant information to its customers. Information about products and services are made available in all three languages, and employees are available to provide further information where necessary. The Bank also conducts events island-wide aimed at educating current and potential customers about products and services.

Focus on Social Responsibility

DFCC Bank offered "Vardhana *Sahanaya*", a DFCC Bank-funded concessionary loan scheme, to rebuild the lives of the public affected by the floods and landslides that took place in 2017. The scheme was offered to both customers and non-customers of the Bank, and was used to rebuild business and personal assets. Facilities under the *"Athwela"* concessionary loan scheme funded by the Government were also offered by the Bank to the business community affected by these natural disasters.

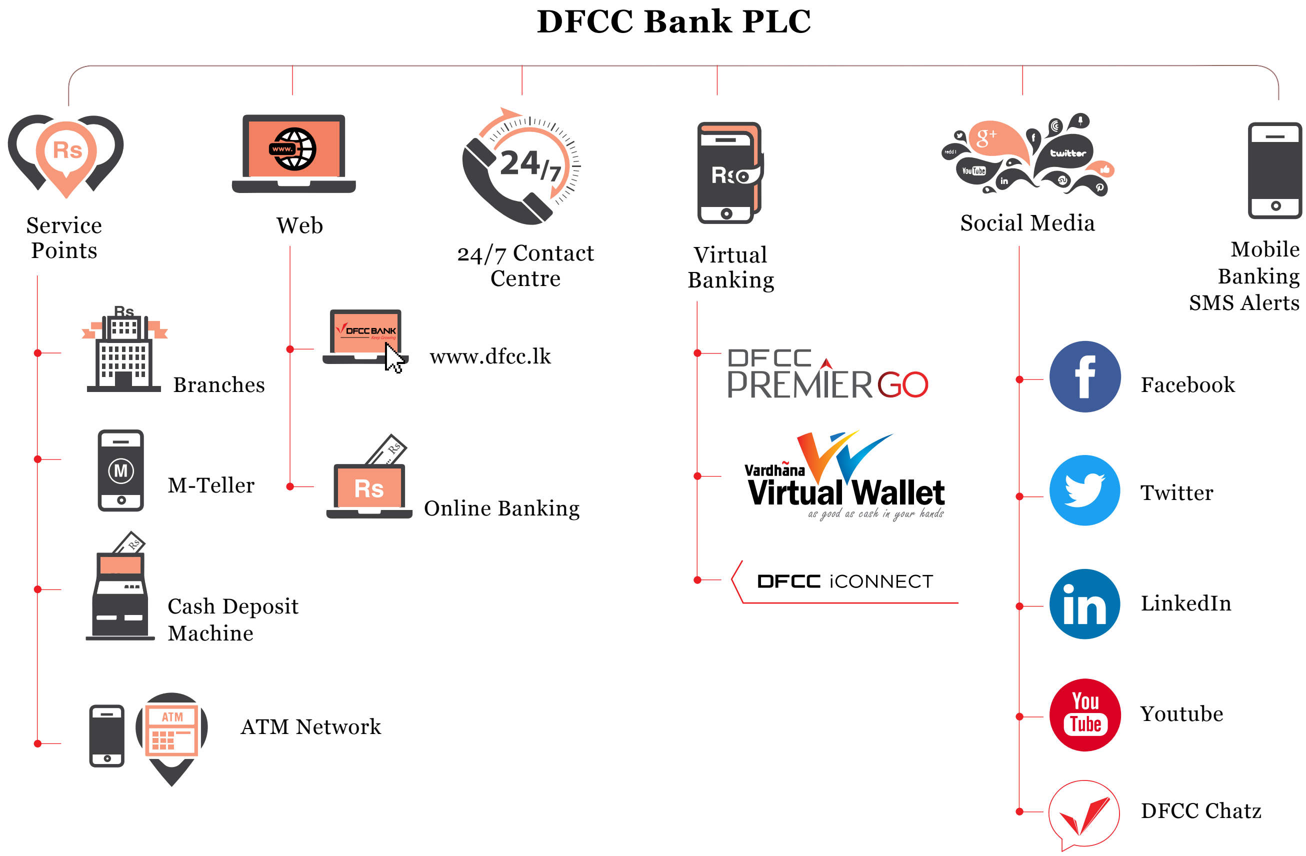
Customer Privacy

DFCC Bank recognises the importance of protecting its customers' privacy as a key component of building trust and developing the relationship between the Bank and its customers. To this extent, the Bank utilises secure systems and procedures throughout banking transactions, and continuously works to develop and upgrade these systems. Moreover, "customer privacy" is an integral part of the employee Code of Conduct, aimed at ensuring that employees recognise the importance of protecting their customers' privacy and continue to uphold the Bank's secure systems and procedures.

Customer Satisfaction and Complaint Handling

The Bank has a wide network of customer touch points ranging from the conventional brick and mortar to Internet and mobile centric digital banking solutions such as "Virtual Wallet" and "Premier Go". Given the fast changing customer aspirations and preferences, it is imperative that the Bank uses banking technology to reach the customer. While some of the customers prefer to continue to bank the conventional way with a human touch, there is a new generation of customers who demand a contextual banking experience. The Bank will continue to innovate ways and means of increasing its reach further.

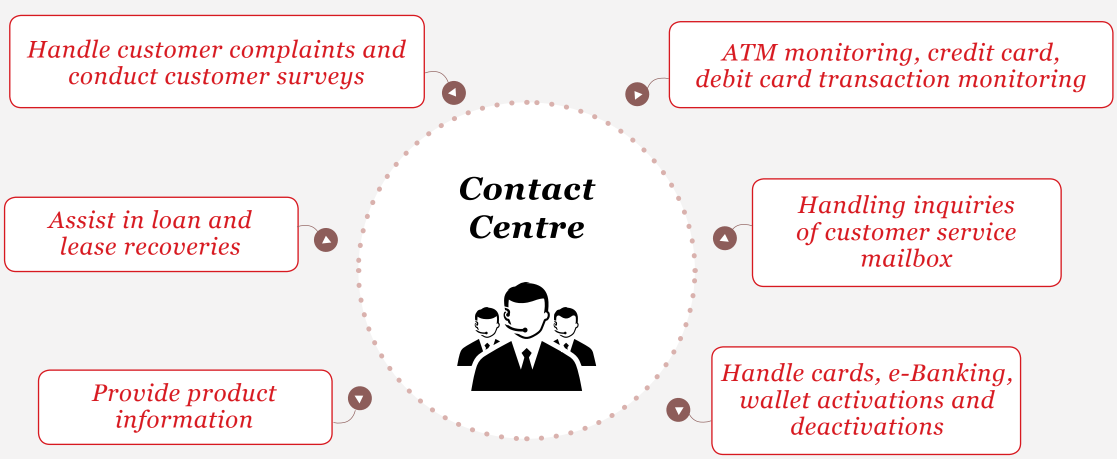
Multi–Channel Customer Touch points



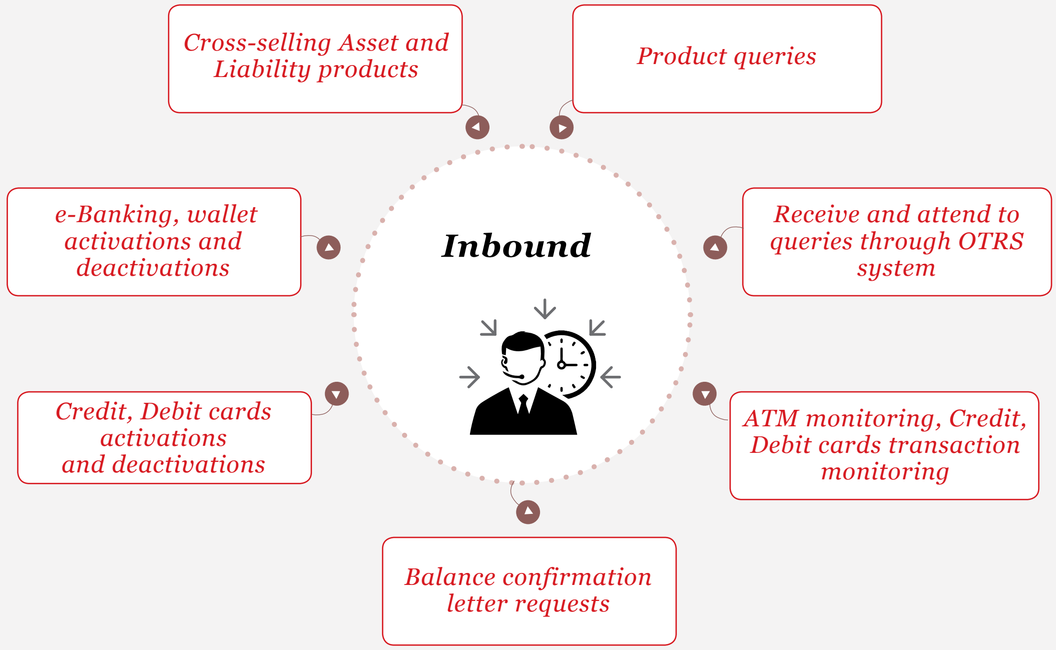
Contact Centre

Operating under the Alternate Channels Department, the Contact Centre is an important service provider as a channel that acts as the first point of contact for customers who call the Bank. The Contact Centre conducts both inbound and outbound functions and operates 24 hours, seven days a week to ensure the smooth functioning of the Bank's operations.

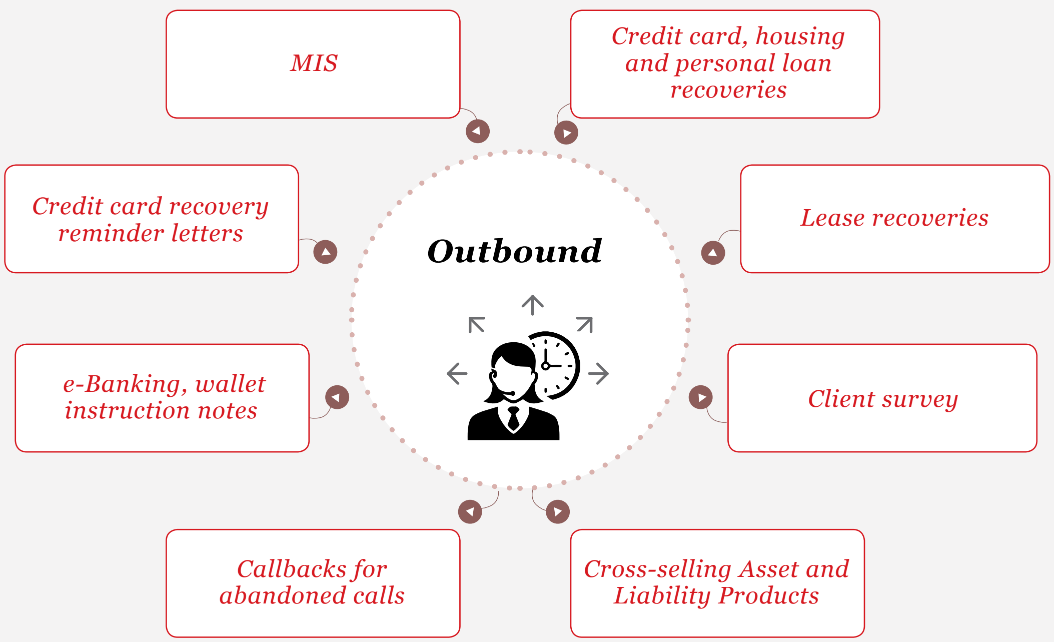
Core Responsibilities of Contact Centre



Inbound Operations



Outbound Operations



Handling Product Queries and Activations

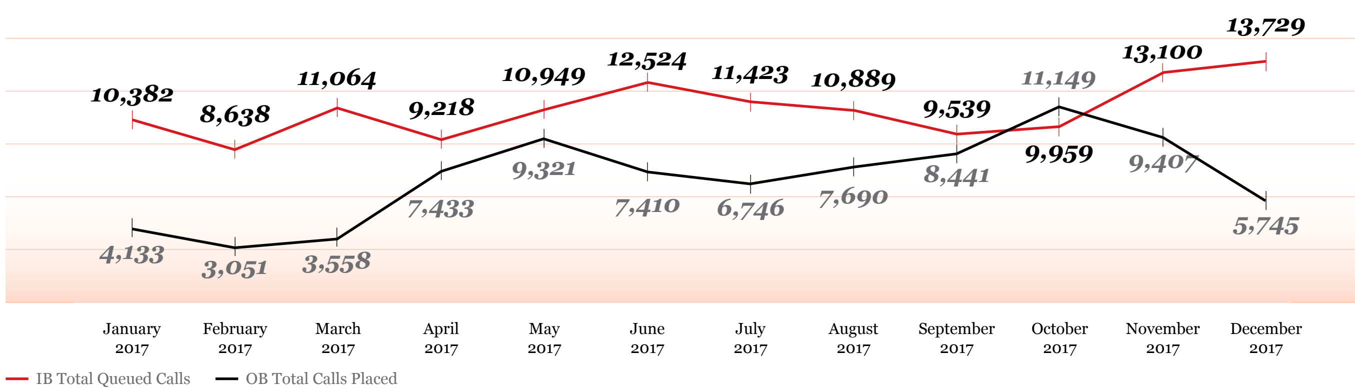
Contact Centre staff members are trained and coached on the Bank's products, and receive briefings whenever a new product or system is launched. A comprehensive customer validation methodology has been adopted and is conducted prior to providing any information to customers.

Summary of Inbound and Outbound calls

Inbound 2017	Duo system			Facetone system								
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Total queued calls	10,382	8,638	11,064	9,218	10,949	12,524	11,423	10,889	9,539	9,959	13,100	13,729
Total answered calls	9,427	7,762	9,848	8,227	10,237	11,379	9,958	9,288	8,194	9,317	11,922	12,872
Average answered calls per day	304	277	318	274	330	379	321	300	273	301	397	415
Average talk time (Sec.)	148	142	148	163	172	128	108	119	116	199	129	124
Average ACW time (Sec.)	7	7	5	22	19	17	14	13	0	16	11	10
Average answer time (Sec.)	**–**	**–**	**–**	**10**	**9**	**8**	**9**	**9**	**2**	**10**	**7**	**7**

Outbound 2017	Duo system			Facetone system								
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Total calls placed	4,133	3,051	3,558	7,433	9,321	7,410	6,746	7,690	8,441	11,149	9,407	5,745
Average calls placed per day (Week days)	197	170	155	437	466	371	321	350	444	557	448	302
Average talk time (Sec.)	**–**	**–**	**–**	**–**	**–**	**53**	**47**	**54**	**54**	**60**	**63**	**72**

Trend of Calls – Nos.



Complaint Management through OTRS

The Call Centre monitors complaints received through the hotline, complaints line, and customer service mailbox. If a resolution cannot be provided by the Call Centre on the first attempt to address a complaint, it is escalated to the relevant department, branch, or the Management, and at the end of each month, a report consisting of the total complaints received (IRM Report) is sent to the Operational Risk Manager of the Integrated Risk Management Department.

Causes of complaints are identified under three categories, and the number of complaints received under each category are depicted in the following table:

Complaints Summary

Process	9
Staff	5
Technology	75

Summary of Complaints Received During the Year

- Two complaints were received on loans disbursement. These indirectly affected the Bank's reputation as customers were disappointed that their loan applications were not successful within the expected time period. Irregularities in loan disbursements and miscommunication with potential loan clients led to these complaints.
- Eight complaints were received due to a lack of knowledge in banking operations and non-adherence to the standard operational procedures laid down by the Bank. Some of these complaints were mainly due to lapses in the service offered to customers and the lack of professionalism with which situations had been handled.
- Six complaints were received due to technological issues. These can normally occur in banking operations, but are not considered acceptable by customers. Examples of such issues included receiving several emails after online banking transactions, delays in updating credit card payments, deduction of extra charges for accounts (WHT), and delays in renewal notices of fixed deposits.

15

One new branch and 14 extension offices converted to fully-fledged branches

13%

growth in personal loans

44%

year-on-year growth in institutional deposits

13.1%

year-on-year growth in import/export volumes

- One complaint was received as a result of the disclosure of a customer's facility details to a third party.
- Two complaints were received due to the return of cheques without the customer receiving prior notification.

Additionally, issues that did not fall into the aforementioned categories are listed below:

Not a Complaint	***43***
Validation Errors	***110***
Actual Service Failures	***261***
Unsuccessful Transactions	***388***

- Not a complaint: complaints received from an unsatisfied customer despite the Bank having performed its services successfully. (e.g. Debit card PIN has not been received, but was duly dispatched by the Bank to the correct mailing address) 43 complaints were received.
- Validation errors: Incorrect information that has been input into the co-banking system. (e.g. Incorrect NIC number, incorrect residence address and incorrect name in the EOC system). 131 complaints were received.
- Actual service: Service lapses and violation of service level standards are considered as actual service failures. 275 service failures were reported.
- Unsuccessful transactions: Complaints received about ATM withdrawals that were debited from the customer's account but not received by the customer are considered as unsuccessful transactions. Out of 388 complaints, six transactions are still under pending status as at 31 December 2017. 70 complaints related to DFCC Virtual Wallet promotions were received. These complaints were due to merchant service level agreement failures, merchant system issues and DFCC Virtual Wallet system failures. Refunds have been given to all these customers who encountered issues and needed settlement.

Marketing Communications

The Bank undertook several brand-building initiatives during the course of the year, including marketing and seasonal campaigns, event sponsorships, and customer engagement activities.

Through a Board approved Corporate Communications Policy and Social Media Policy, the Bank engages with customers and potential customers over multiple channels of communication in English, Sinhala, and Tamil. The Bank takes every effort to ensure the accuracy of information and compliance with the CBSL and the Bank's Customer Charter.

...serving customers...

DFCC products are tailor made to meet customers' personal requirements. We are enhancing systems and processes that allow customers to enjoy a more individualised portfolio of financial lifestyle solutions, improving accessibility through digital banking, a 24 hour contact centre and an island-wide branch footprint.

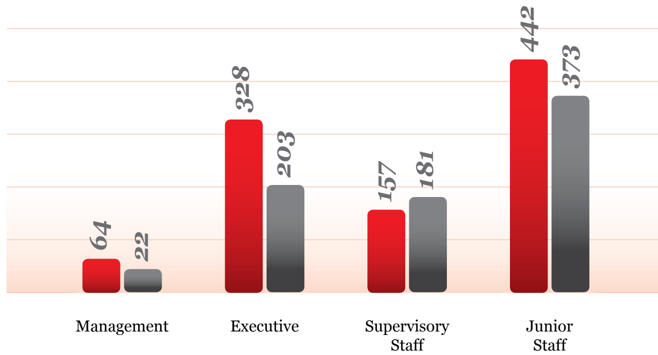
EMPLOYEE CAPITAL

DFCC Bank grew its Human Capital base to 1,770 in 2017 – an increase of 7% over 2016 - with permanent employees accounting for 80%. The gender distribution ratio, stood at 56:44 (male to female), whilst in relation to age distribution, employees under 30 years of age comprise 57.6% of the overall headcount.

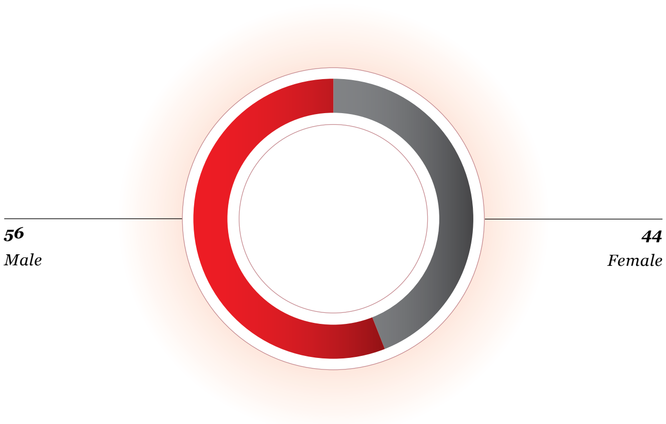
56% of employees were stationed in the Western Province, followed by 9.7% in the Southern Province and 8.5% in the Central Province. The Northern and Eastern Provinces, with 10 branches accounted for 8% of the total workforce.

Staff Analysis

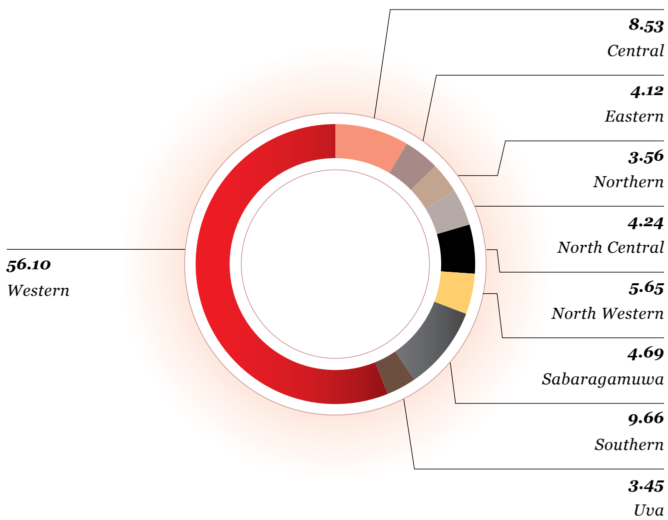
Staff Distribution by Category – Nos.



Staff Distribution by Gender – %



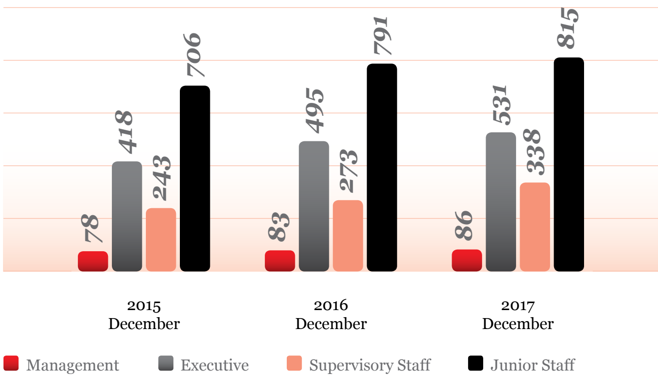
Employees by Province – %



Workforce by Employment Type/Contract and Gender

Grade	Permanent			Contract/Casual/Part time			Total Number of Employees		
	Male	Female	Total	Male	Female	Total	Male	Female	Total
Management	53	19	72	11	3	14	64	22	86
Executive	295	190	485	33	13	46	328	203	531
Supervisory Staff	156	181	337	1	0	1	157	181	338
Junior Staff	246	269	515	196	104	300	442	373	815
Total	**750**	**659**	**1,409**	**241**	**120**	**361**	**991**	**779**	**1,770**

Change in Total Headcount – Nos.



Total Workforce by Region and Gender

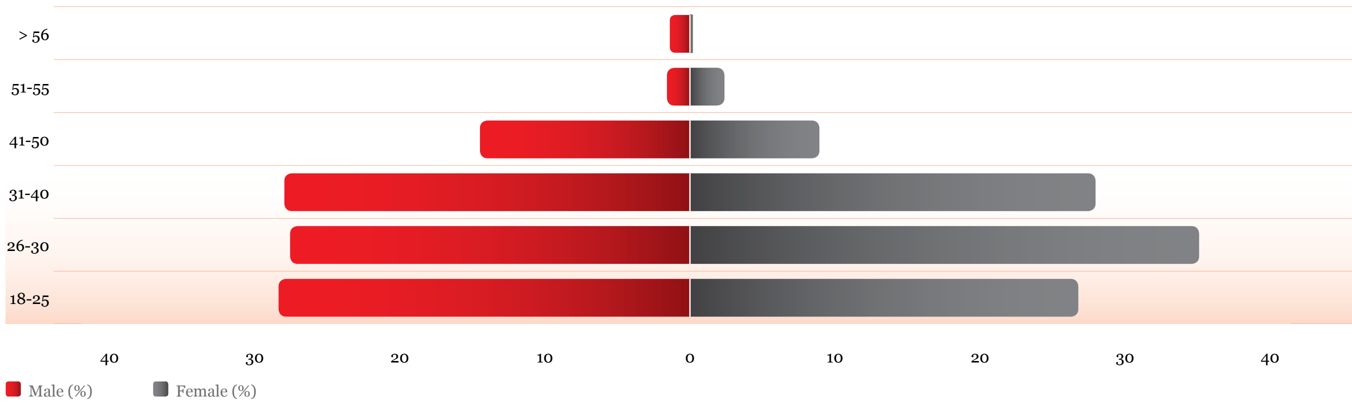
Province/Departments and Other Business Units	**2017 December**					2016 December					2015 December				
	No. of Employees					No. of Employees					No. of Employees				
	No. of Branches/ Departments	**No. of SLP Units**	**Male**	**Female**	**Total**	No. of Branches/ Departments	No. of SLP Units	Male	Female	Total	No. of Branches/ Departments	No. of SLP Units	Male	Female	Total
Central	**13**	**2**	**105**	**46**	**151**	11	4	95	45	140	10	4	69	47	116
Eastern	**8**	**2**	**55**	**18**	**73**	8	2	52	21	73	7	4	50	22	72
Northern	**6**	**0**	**39**	**24**	**63**	6	0	38	23	61	6	0	34	21	55
North-Central	**6**	**3**	**52**	**23**	**75**	6	3	50	25	75	3	6	42	20	62
North-Western	**9**	**2**	**58**	**42**	**100**	7	3	51	46	97	6	4	36	38	74
Sabaragamuwa	**7**	**8**	**48**	**35**	**83**	7	8	43	40	83	5	10	36	35	71
Southern	**15**	**8**	**98**	**73**	**171**	9	14	72	73	145	9	14	67	67	134
Uva	**4**	**5**	**40**	**21**	**61**	4	5	38	19	57	4	5	38	18	56
Western	**33**	**7**	**213**	**192**	**405**	32	8	185	188	373	29	11	146	176	322
Departments and Other Business Units	**76**	**0**	**283**	**305**	**588**	69	0	250	288	538	63	0	208	275	483
Total	**177**	**37**	**991**	**779**	**1,770**	159	47	874	768	1,642	142	58	726	719	1,445

Note : Number of staff attached to Regional offices are included with respective province staff count

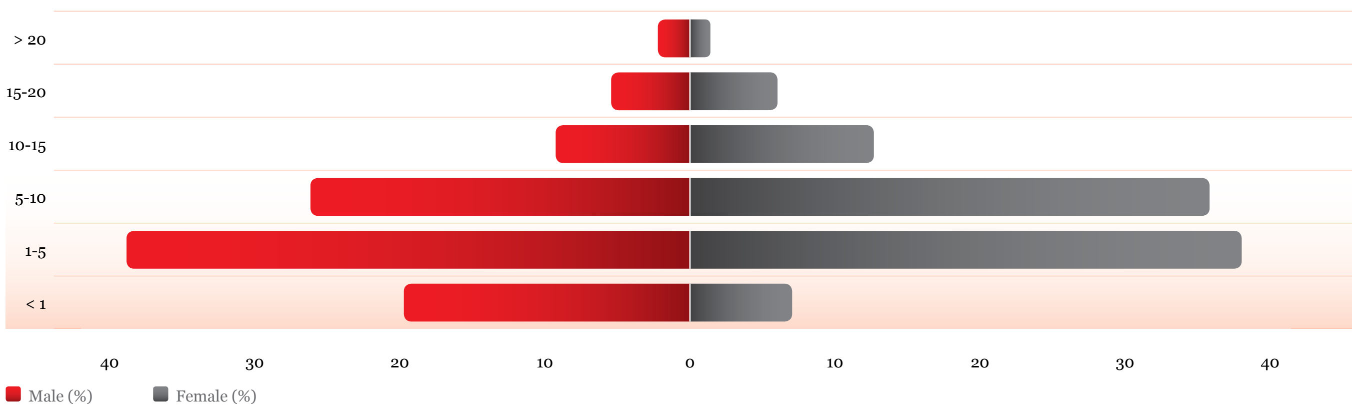
Workforce by Age and Category

Grade	Management		Executive		Supervisory		Junior Staff	
	Count	%	Count	%	Count	%	Count	%
18-25	0	0	12	2	1	0	469	58
26-30	0	0	143	27	121	36	275	34
31-40	8	9	267	50	169	50	45	6
41-50	53	62	99	19	40	12	18	2
51-55	16	19	8	2	6	2	4	0
56 +	9	10	2	0	1	0	4	0
Total	**86**	**100**	**531**	**100**	**338**	**100**	**815**	**100**

Age Pyramid – Years



Seniority Pyramid – Years



Development and Growth

As per the Bank's emphasis on investing in employees, extensive opportunities to receive training and development were provided during the year.

Grade	No. of person hours of training Male	Female	Total
Management	2,031	590	2,620
Executive	11,806	7,191	18,997
Non-Executive	16,298	13,198	29,496
Total	**30,134**	**20,979**	**51,113**

** Excluding e-learning*

	Total person hours 2017
In house	46,211
External	4,306
Foreign	596
E-learning	21,552
Total	**72,665**

Development needs are identified via different means, including:

- Individual development plans prepared by supervisors upon discussion with their employees
- Discussions with cross functional groups
- Discussions with business heads

Once identified, the needs are addressed through:

- Provision of classroom-based training opportunities (domestic and overseas)
- On-the-job training
- Job rotations
- Role enhancements
- Special assignments
- e-learning opportunities

The Bank's e-learning platform which offers relevant business and soft skill-based content, was widely used to deliver knowledge to employees across the country as well as conduct assessments and quizzes to ensure an effective and fun learning experience. Usage of the platform grew by 22%. User satisfaction was aptly demonstrated at the annual survey which noted that 99% of users were highly satisfied with the facility provided.

In 2017, 404 training programmes were conducted of which 178 were conducted in-house – a 22% increase over the previous year's in-house offerings. Nearly 72,700 hours of training were provided during the year, with employees receiving an average of 42.6 hours.

Improving the continuous development and progression of employees remained a priority for the Bank. During the year, 70 junior level employees underwent the Officer in Charge (OIC) Certification Programme, with 47 participants successfully completing the stringent course, a prerequisite to perform an OIC role at the Bank. Since its inception, 161 employees have being successfully certified. A Credit Certification Programme, was introduced this year to assist junior level staff to embark on a career path in credit, with 24 staff participating in the seven day programme, and 50% successfully completing the certification process.

The individual-focused career development programmes, "Ascension" (targeting high potential staff) and "Rise" (aimed at staff requiring focused assistance to perform at expected levels), continued to be rolled out in 2017. Currently 32 employees are participating in the Ascension programme, and 16 employees in the Rise programme.

The re-skilling programme, introduced in 2016, aims to enable mature employees, whose job roles have changed based on business needs, to acquire the relevant knowledge and skills required to perform their new roles optimally. The programme continued to be rolled out in 2017 with progress regularly monitored and interventions made when necessary. With this focused attention it is noteworthy that 12 of the 46 participating employees left the programme, having achieved their expected performance levels.

Coaching and mentoring initiatives were offered to employees, based on individual needs during the year. Additionally, new employees were assisted to assimilate quicker into the work environment through on-boarding programmes and the "Buddy Scheme". The Buddy Scheme sees senior colleagues act as buddies to the new recruits, helping them to understand the Bank culture, policies, practices, and the expectations of their job roles. Further demonstrating continued commitment towards assisting employees with their personal and professional ambitions, the Bank offers varied assistance and grant schemes for higher education. During the year under review, 156 employees took advantage of these schemes.

Recruitment and Retention

Recruitment

During 2017, the employee base grew by 319, necessitated by the continued expansion of the branch network and introduction of new business offerings and services. Of the new recruits, 68% were for junior level positions, while 78% of them were under the age of 30. The Bank maintained its commitment to having internal talent groomed to take on more responsibility in the future, with only one external recruitment being made to a management position during the year. Resourcing talent with the desired level of competency and the right fit continued to be a key HR challenge during the year, with sales roles being particularly challenging to fill despite attractive incentive schemes and the availability of dedicated and progressive career paths.

Grade	New Employees Joining in the Current Financial Year						
	Age Group				Gender		
	Less than 30 Years	Between 30-50 Years	Above 50 Years	Total	Male	Female	Total
Management	0	1	0	1	1	0	1
Executive	33	41	0	74	59	15	74
Supervisory Staff	10	15	0	25	22	3	25
Junior Staff	205	12	2	219	163	56	219
Total	**248**	**69**	**2**	**319**	**245**	**74**	**319**

2017 saw 66% of new hires sourced for branches, with the majority of hires to the Southern Province, as six of the 14 new branches opened during the year were in this region.

New Hires by Province

Province	Total
Central	23
East	10
North	9
North-Central	13
North-Western	14
Sabaragamuwa	19
South	43
Uva	14
Western	174
Total	**319**

Retention

83 permanent employees voluntarily resigned during the year, 42% of whom were junior staff. Retention of sales staff continued to be a challenge, with the year seeing 52 such staff leaving the Bank. Exit interviews are conducted for resigning permanent staff members, with appropriate feedback given to their supervisors and other corrective actions taken, if warranted. The Operations Risk Management Committee reviews attrition data on a quarterly basis, highlighting the importance of human capital to the Bank. The attrition rate of permanent employees in 2017 was to 6.1%.

Total Number and Percentage of Employee Turnover by Age Group and Gender

Category	**2017 December**				2016 December				2015 December			
	Employee Turnover		**%***		Employee Turnover		%*		Employee Turnover		%*	
	Male	**Female**	**Male**	**Female**	Male	Female	Male	Female	Male	Female	Male	Female
Below 30 Years	**20**	**19**	**7**	**6**	23	19	8	6	20	28	7	8
30 – 50 Years	**23**	**21**	**5**	**6**	20	15	5	5	19	14	6	5
51 – 60 Years	**0**	**0**	**0**	**0**	2	0	13	0	0	1	0	11
Above 60	**0**	**0**	**0**	**0**	0	0	0	0	0	0	0	0
Total	**43**	**40**	**6**	**6**	45	34	7	5	39	43	6	7

** As a percentage of total male/female staff in each employee category in the permanent cadre*

Number of Employees Resigned

Category	Age Group				Gender		
	Less than 30 Years	Between 30-50 Years	Above 50 Years	Total	Male	Female	Total
Management	0	1	0	1	1	0	1
Executive	5	23	0	28	14	14	28
Supervisory Staff	5	14	0	19	9	10	19
Junior Staff	29	6	0	35	19	16	35
Total	**39**	**44**	**0**	**83**	**43**	**40**	**83**

Resignations by Province

Province	Total
Central	5
East	0
North	3
North-Central	5
North-Western	5
Sabaragamuwa	3
South	8
Uva	2
Western	52
Total	**83**

Return to Work after Parental Leave

Indicator	Male	Female	Total
Number of employees entitled to parental leave during previous reporting period (2016)	n/a	768	768
Number of employees who took parental leave and due to return during 2017	n/a	59	59
Number of employees who returned to work after parental leave during 2017	n/a	57	57
Employees who returned to work out of those due to return during 2017	n/a	97%	97%
Number of employees due to return to work after parental leave during 2016	n/a	67	67
Number of employees who returned to work after parental leave during 2016	n/a	66	66
Employees who returned to work out of those due to return during 2016	n/a	99%	99%
Number of employees who returned to work after parental leave during 2016, who were still employed 12 months after return to work	n/a	58	58
Retention rate	n/a	87%	87%

Benefits

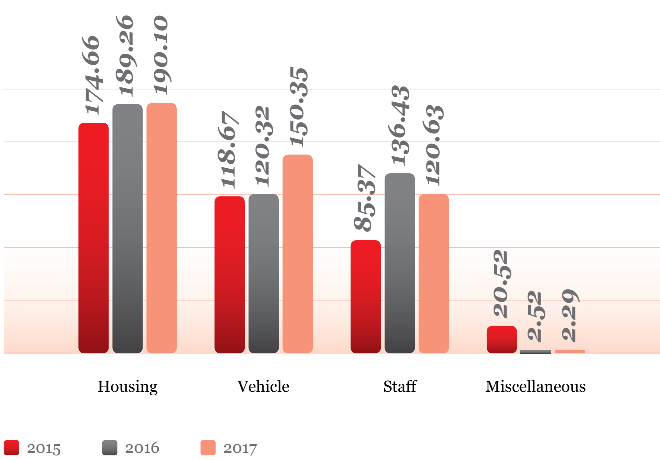
Employment Type	Permanent	Contract
Housing Loan	√	x
Vehicle Loan	√	x
Exam*	√	x
Professional Subscription*	√	x
Social Club Gymnasium*	√	x
Miscellaneous/Staff Loan	√	x
Festival Advance**	√	x
MBA Loan	√	x
Holiday Grant***	√	x

* *Executive Trainees and Management Trainees on fixed term contracts will also be provided*

** *Only for non-executive staff*

*** *Based on the offer of employment, may be provided to the contract staff as well*

Loan Utilisation – *LKR million*

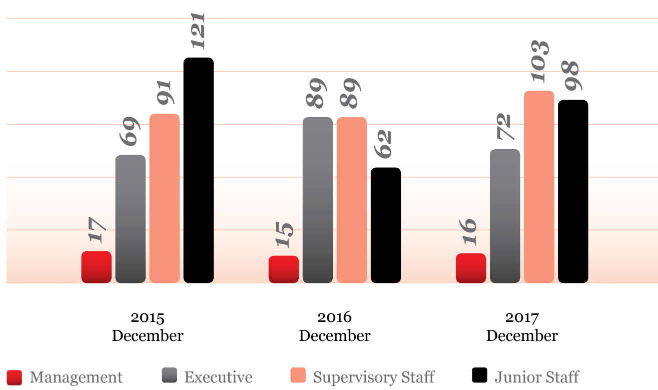


Performance Management

Performance management continued to have key focus. Formal performance reviews were conducted mid-year and year-end, although supervisors are encouraged to conduct more frequent reviews. At the year-end evaluation, based on achievement of targets, employees are individually assessed and performance based bonus and annual increments awarded. The performance assessments are affiliated to the promotion mechanisms of the Bank as well.

Employees also have the option to escalate their concerns, in the case of disagreement over the performance evaluation, to the HR department, the Grievance Committee, and even the CEO.

Staff Promoted – *Nos.*



Work Life Integration

DFCC Bank promotes work life integration and an environment which encourages staff to participate in extra-curricular hobbies and passions outside of their job scopes. To this end, groups such as the Welfare and Recreation Club, DFCC REDS, Mess Committee, and DFCC Community Projects Team organised different initiatives throughout the year, aimed at promoting interaction among employees and their families, enhancing health and wellness, and providing employees with opportunities to contribute to the larger community.

This year's annual dance witnessed its largest patronage yet, with 1,300 employees and their families participating. Events such as overnight trips, the sports day, cricket matches, the Christmas party and carols, quiz nights, and mess nights provided employees with a multitude of opportunities to mix and mingle.

Focus continued to be placed on employee wellness, with programmes being held on non-communicable diseases, health and fitness and advice on nutrition, exercise, and mental wellness also being regularly disseminated. Activities, including hiking trips, yoga classes, a pedometer challenge, a six-month boot camp programme, and a free medical camp for staff were organised throughout the year. The Bank continued to invest in sports activities such as basketball, badminton, and tennis, while also sponsoring employees to participate in local and international sports competitions. The Bank also provides fully and partially sponsored gym and social club memberships, a benefit utilised by 195 employees during the year.

In keeping with one of the Bank's core values of being "socially responsible", employees participated in many events including an annual blood drive, a beach clean-up, donations to orphanages, a fully funded day out for 60 students from an underprivileged school and a public eye donation campaign conducted on behalf of the National Eye Bank of Sri Lanka with over 300 donors signing up. The DFCC REDS closed the year's employee-initiated CSR projects by organising school supplies to assist children from underprivileged backgrounds. When significant segments of the community were impacted by inclement weather, the Bank carried out disaster relief efforts with the active engagement of the staff. The Bank, along with its employees, generously donated funds to assist impacted colleagues and the larger community. Employees also contributed their time and effort to prepare ration packs for victims, assist at medical camps organised by the Bank in Akuressa and Deniyaya, and contributed towards the clean up and reconstruction efforts of six affected schools.

Grievance Redressal

DFCC Bank's employees have many avenues through which they can raise concerns and seek redressal. The Board-approved Grievance Policy outlines the grievance escalation process, while a Grievance Committee, comprising cross-functional representation of employees, is available to raise concerns. The Bank's secure Environment Policy clearly outlines and advocates for a harassment-free environment that provides equal opportunities for all, and outlines mechanisms and options to address issues.

The "Reach Out" programme, launched during the latter part of 2016, provides a platform for female employees to seek assistance on personal and professional issues that affect them. Periodically organised open days with the Chairman and CEO, and access to their dedicated phone lines and email addresses give employees access to the highest level to address their grievances.

A majority of the grievances raised during the year pertained to transfers, performance evaluations, and promotions. The Grievance Committee held quarterly meetings to discuss common issues raised with them and receive updates on issues raised with HR. Grievances received under the Reach Out programme were all appropriately addressed.

1,770
Total headcount in 2017

319
new recruitments in 2017

72,700 hours
of staff training

Over 1,100
merchants connected to the DFCC Virtual Wallet

Over 250
global correspondent banks

Thanking and Rewarding

The Bank recognises the pivotal role of appreciation and recognition towards employee engagement, productivity, and retention. Several programmes are offered to promote these aspects within the Bank's workplace ethos.

Through the "Rewarding Excellence" scheme introduced in 2013, the special and extra contributions of employees continue to be recognised – the achievements of 41 employees were celebrated during the year with active participation from members of the Board of Directors and senior management. Since the inception of the scheme, 113 employees have been recognised and rewarded.

An "Appreciation Night" was held in 2017 to thank over a hundred employees who regularly and voluntarily took on additional roles and responsibilities for which they are not monetarily compensated. An "Awards Night" was introduced for the first time in 2017, with employees recognised for business and sales performance, and awards given for excellence in areas such as sports, customer service, volunteering, and many other aspects.

An e-card platform was introduced this year to provide employees with a quick and convenient system to recognise and appreciate specific contributions of their colleagues, subordinates, and supervisors.

Embracing Diversity, Inclusion and Equality

The Bank has strived to ensure fair and equitable workplace policies and practices, irrespective of gender, cultural or religious diversity. The tables below demonstrate the Bank's commitment towards ensuring equitability.

Ratio of Salary of Men to Women by Employee Category

	2017			
	Male	Female	Total	Basic Salary ratio, Male/Female
Management	64	22	86	46:54
Executive	328	203	531	51:49
Supervisor	157	181	338	51:49
Junior Staff	442	373	815	49:51
Total	**991**	**779**	**1,770**	**49:51**

Promotions by Gender – *Nos.*

Recognition and celebration of cultural diversity was demonstrated throughout the year, with employees organising and celebrating multi-religious and cultural events, and enthusiastically decorating their workspaces to commemorate these events, irrespective of their own personal religious and cultural affiliations.

Occupational Safety

DFCC Bank is committed towards occupational safety and measures are in place to prevent accidents and injuries in the workplace. Due to the nature of the work, the Bank employees are not generally subject to major injuries or hazardous substances. All premises of the Bank are considered non-smoking zones. The Bank also takes measures to regularly educate employees on occupational safety, health and related subjects. In 2017, programmes were conducted on first aid and fire evacuation while employees continued to be educated on how to deal with unplanned events. Two employees experienced minor injuries in the workplace, and the Bank responded by implementing measures to rectify the situation and ensure that such situations would not recur.

Collective Agreements

Due to the absence of employee unions, the Bank does not have a requirement for collective agreements. Market surveys are conducted every three years, as per the Remuneration Policy, to benchmark employee remuneration levels against that of competitors. Based on survey feedback and affordability considerations, adjustments are made to salary and benefits.

BUSINESS PARTNER CAPITAL

Multilateral and Bilateral Institutions

Since its inception, DFCC Bank has developed and nurtured strong relationships with many multilateral and bilateral institutions that share similar goals. Business partners include:

- The World Bank
- European Investment Bank (EIB)
- Asian Development Bank (ADB)
- Kreditanstalt fur Wiederaufbau (KfW) – Germany
- Deutsche Investitions-und Entwicklungsgesellschaft (DEG), a subsidiary of KfW – Germany
- Nederlandse Financierings – Maatschappij voor Ontwikkelingslanden N.V. (FMO) – Netherlands
- Proparco, a subsidiary of Agence Française de Développement (AFD) – France

DFCC Bank's role in these partnerships is primarily being an effective credit institution for on-lending funds to end users, or acting as the project manager in implementing credit programmes, administering grant funds and smart subsidiaries for market development and capacity building.

In 2016, DFCC Bank made inroads to the Middle Eastern sector for funding requirements. The Bank enjoys a bilateral funding relationship with RAKBANK, also known as the National Bank of Ras Al Khaimah, in the UAE.

During the period under review, DFCC Bank was granted a long-term loan of EUR 20 million by Proparco, a subsidiary of Agence Française de Développement (AFD), further affirming the Bank's reputation as a preferred partner for international credit lines. The Organisation is devoted to private sector financing to finance renewable energy projects and improve access to credit for Small and Medium Enterprises (SMEs) in Sri Lanka.

DFCC Bank prides itself in being one of the premier banking institutions in the country that promotes and supports the operations of Small and Medium Enterprises. During the year, the Bank secured funding of USD 30 million from BlueOrchard, a leading global impact investment manager, to increase lending to SMEs, while strengthening its micro-finance portfolio.

Building upon the relationships the Bank has established over time, the Treasury and Resource Mobilisation Unit actively engages with partner institutions to secure potential funding lines to support the Bank's rapid growth.

Correspondent Banks

The Bank maintains relations with over 250 global correspondent banks. The Bank added new correspondent banking relationships to its network that will facilitate customer transactions which originate in or involve foreign countries. The entities listed below act as the Bank's nostro agents in the respective countries.

Bank	Country
Bank of Ceylon (UK) Limited	UK
Bank of Ceylon	India
Bank of Ceylon	Maldives
Bank of China	China
Commerzbank AG	Germany
Commonwealth Bank of Australia	Australia
Deutsche Bank Trust Company Americas	USA
HDFC Bank	India
HSBC Bank USA N.A.	USA
Kookmin Bank	South Korea
Mashreqbank PSC	India
Mashreqbank PSC	UAE
Mashreqbank PSC	USA
Standard Chartered Bank (Pakistan) Limited	Pakistan
Standard Chartered Bank	Bangladesh
Standard Chartered Bank	Germany
Standard Chartered Bank	India
Standard Chartered Bank	Singapore
Standard Chartered Bank	USA
Sumitomo Mitsui Banking Corporation	Japan
UniCredit Bank AG	Germany
Zurcher Kantonal Bank	Switzerland

The Supply Chain Management and Procurement Policy

DFCC Bank's Procurement Policy provides clear guidance on the procurement of goods and services by authorised staff to ensure fairness, transparency, and accountability for decisions. The policy ensures that the selection of suppliers and the acquisition of goods and services are done in a non-discriminatory, transparent, and economically sound manner.

A Procurement Committee (PC) led by an Executive Vice President serves as a control measure to the procurement function of the Bank. All recurrent procurements are performed according to the Board approved Delegated Authority Circular in force. All major IT-related procurements are submitted to an IT Steering Committee (ITSC) and referred for PC approval, with the recommendation of the ITSC. Other general procurements are submitted either to the PC for approval, or to higher approving authorities, with the recommendation of the PC. Large value and/or specialised procurements may be subject to a further review by an independent party, if deemed necessary.

Suppliers of goods and services have to register centrally with the approval of the PC, after which the Delegation of Authority for Capital and Revenue Expenditure will become effective. Registered suppliers are subject to review once every two years.

The selection of suppliers entails a rigorous process wherein the three "rights" are evaluated: the right quality, the right time (delivery), and the right price. Other aspects that are evaluated include after sales support, acceptable references, and technical proficiency.

With a preference for procuring from local suppliers, DFCC Bank honours its commitment to helping local communities flourish. Suppliers may receive financial advice and assistance from the Bank, if they require.

The Bank always attempts to maintain optimum stock levels in order to avoid unnecessary storage costs/space requirements.

Members of the Board of Directors and employees who are involved in initiating a procurement or are in an evaluation panel are required to disclose any interest they may have in any procurement decision under consideration or evaluation, and cannot participate in the decision-making process. The Bank does not carry out purchases on behalf of employees.

Partners for Service Delivery

DFCC Bank works with several reputable vendors for various services, including:

- Cash collection, counting, storage, delivery and transport of security goods
- Printing of account and credit card statements, printing cheque books, personalisation and dispatch services
- Processing of payroll and other reimbursements
- Personalisation of chip-based credit cards
- Delivery of personalised credit cards
- Internal audit functions such as monitoring and compliance with existing internal control procedures, reporting on non-compliance/control gaps and offering recommendations
- IT support, issues of warranty, maintenance calls, time and material services, and software issues related to the Bank
- Help desk problem management, hardware and software handling and general queries
- The Bank also has relationships with over 1,100 merchants, ranging from online stores, grocery stores to hospitals, participating in the DFCC Virtual Wallet. Further details can be found under Industry Initiatives on page 76.

Industry Initiatives

Lanka Money Transfer (LMT)

Lanka Money Transfer (LMT) is a state-of-the-art remittance system which enables instant remittances to accounts maintained in DFCC Bank PLC and any LMT Partner Bank/Financial Institution via a secure network. Through this service, migrant workers are able to remit their earnings to their loved ones back home in a secure and speedy manner. The funds will be credited to the beneficiary's account held at DFCC Bank or any other account held with LMT Partner Banks/Financial Institutions with minimal hassle. For this purpose, DFCC Bank has ensured it houses the best exchange companies under one roof.

LMT is currently operating with 11 exchange companies in UAE, Qatar, Oman, South Korea, Israel, and Australia, and partnering with 11 financial institutions in Sri Lanka.

Exchange Companies include Future Exchange LLC, Al Ansari Exchange LLC, Lulu International Exchange LLC, Sharaf Exchange LLC, Al Zaman Exchange WLL, Islamic Exchange Co WLL, City Exchange Co WLL, Global Money Exchange Co, Kookmin Bank, Wic Worldcom Finance Limited, and Kapruka Pty Limited.

LMT Partner Banks/Financial Institutions include DFCC Bank PLC, Amãna Bank, HDFC Bank, Regional Development Bank (RDB), Sanasa Development Bank, Union Bank, Pan Asia Bank, Hatton National Bank (HNB), Lanka Orix Finance Company, Citizen Development Bank, and Sarvodaya Development Finance.

DFCC Bank PLC has commenced work to expand LMT Operations to other destinations and looks forward to having arrangements in all potential destinations by Q2 of 2018.

DFCC Virtual Wallet

The DFCC Virtual Wallet, an innovative mobile payment solution which was introduced in 2016, reported a rapidly captivated audience during 2017. With its continuous new developments, the services were extended to all mobile subscribers and non-account holders as well.

At the end of 2017, over 10,000 customers and 1,100 merchants were using the mobile payment solution. To add convenience to its users, new features such as DFCC Chatz which helps all customer queries answered via the Bank Facebook Page and voice command feature to make payments, check balance and transfer funds via the voice command, were introduced.

DFCC "Premier Go"

DFCC Bank launched "Premier Go", the first ever premier banking app in the industry, exclusively for the Bank's premier customers in November 2017.

The unique feature of the app is that it enables the customer to contact their Relationship Manager at the click of a button via video conferencing. In addition, it enables the customer to be informed about all their financial information and transactions related to their DFCC premier account in a secure manner.

Payment and Cash Management Solution – DFCC i-Connect

Leading the banking industry in pioneering Fintech solutions, DFCC Bank launched DFCC i-Connect, a fully integrated Payments and Cash Management (PCM) system for the convenience of its customers. DFCC i-Connect offers a range of corporate transactions banking products and services across a unified portal with corporate payments, utility bill payments, corporate collections reporting including virtual accounts, financial supply chain management and a corporate mobile app.

Strategic Alliances

Through a series of strategic acquisitions, alliances, and partnerships over time, DFCC Bank has diversified itself into several entities.

The DFCC Group currently comprises of its subsidiaries:

- DFCC Consulting (Pvt) Limited
- Lanka Industrial Estates Limited
- Synapsys Limited
- Acuity Partners (Pvt) Limited (Joint Venture)
- National Asset Management Limited (Associate company)

Through the combination of these entities, the Group is able to provide a range of services to the financial sector.

DFCC Consulting (Pvt) Limited

DFCC Consulting (Pvt) Limited, established in 2004, is a fully-owned subsidiary of DFCC Bank that engages in project consultancy and related fields. Through its shared resources model, DFCC Consulting draws upon a multidisciplinary, highly-skilled resource pool of nearly 600 executive staff of DFCC Bank, and a pool of reputed external individuals who are experts in various fields. The company provides support to DFCC Bank through its expertise in the fields of environment, engineering, and renewable energy, and carries out international consultancy assignments, sometimes in partnership with overseas consulting firms.

Lanka Industrial Estates Limited (LINDEL)

Lanka Industrial Estates Limited (LINDEL), occupies a strategic location in Sapugaskanda on 125 acres of land. Located in close proximity to the Colombo Harbour and Bandaranaike International Airport, the industrial estate offers land and buildings for lease, and the infrastructure to set up industries. 95% of the leasable land has been let to industries. Twenty production facilities currently operate at the premises, six of which are owned by Fortune 500 companies.

Synapsys Limited

Synapsys Limited, established in 2006, is a fully-owned subsidiary of DFCC Bank that provides software development, MIS solutions, and IT support to DFCC Bank and other customers. The dynamic technology firm, with its array of innovative products and services, including two flagship and NBQSA award-winning platforms, supports banks, capital markets, insurance, and retail payments across Asia and the Pacific Region.

Acuity Partners (Pvt) Limited

Acuity Partners (Pvt) Limited, a joint venture between DFCC Bank and Hatton National Bank (HNB), is the only integrated, fully-fledged investment bank in Sri Lanka. Acuity Partners offers a wide range of products and services in fixed income securities, stock brokering, corporate finance, margin trading, asset management, and venture capital financing.

The following subsidiaries, associates and business units fall under Acuity Partners:

- Acuity Corporate Finance: Provides corporate finance and advisory services
- Acuity Securities Limited: A primary dealer for Government Securities
- Acuity Stockbrokers (Pvt) Limited: A member of the Colombo Stock Exchange
- Lanka Ventures PLC: A venture capital company
- Guardian Acuity Asset Management Limited: A dedicated fund management entity

National Asset Management Limited (NAMAL)

National Asset Management Limited (NAMAL), established in 1991, is the pioneer Unit Trust management company in Sri Lanka. With over 25 years of experience, NAMAL boasts a successful track record of investing in equity and fixed income markets. The Company offers private portfolio management services, and operates eight Unit Trusts, including the first Unit Trust to be licensed in Sri Lanka (National Equity Fund) and the first listed Unit Trust (NAMAL Acuity Value Fund).

Memberships in Industry Associations

DFCC Bank has attained membership and established alliances with several industry associations and organisations. These bring about opportunities for networking and contributing to upholding industry standards, helping to weave a collective voice representing the industry on matters of regulation and policy. The Bank is associated with the following:

- Association of Development Financing Institutions in Asia and the Pacific
- American Chamber of Commerce in Sri Lanka
- The Financial Ombudsman Sri Lanka (Guarantee) Limited
- Association of Compliance Officers of Banks Sri Lanka
- Chartered Institute of Management Accountants
- The Association of Banking Sector Risk Professionals of Sri Lanka
- Chamber of Construction Industry Sri Lanka
- Lanka Fruit and Vegetable Producers, Processors and Exporters Association
- Genesiis Software (Pvt) Limited
- The Ceylon National Chamber of Industries
- The Ceylon Chamber of Commerce
- Mary Martin Book Sellers PTE Limited
- The Institute of Chartered Accountants of Sri Lanka
- The National Chamber of Commerce of Sri Lanka
- The Mercantile Service Provident Society
- Sri Lanka Forex Association
- Reed Business Information Limited
- The Employers’ Federation of Ceylon
- Sri Lanka Banks’ Association (Guarantee) Limited
- Banks CIO Forum
- Lanka Clear (Pvt) Limited
- The Institute of Bankers of Sri Lanka
- The European Chamber of Commerce of Sri Lanka
- International Chamber of Commerce, Sri Lanka

...team spirit...

We have set in place a culture that facilitates team spirit. Keeping in mind the Bank's vision, DFCC's competent and dedicated people work in unison across departments towards the same goal. They are empowered to provide the highest standard of customer service at all times.

SOCIAL AND ENVIRONMENTAL CAPITAL

The sustainability of society and the environment are built into the core values and strategy of the Bank. Thus, the Bank enlists all its resources and encourages its employees to address social and environmental issues, and to engage in community development efforts. Issues and concerns regarding the society and environment can always be escalated to the Bank's Management and Board of Directors.

Social Capital

Socioeconomic Impact

Since its inception in 1955, DFCC Bank has supported economic development initiatives in Sri Lanka and transformed rural economies, enhanced livelihoods, generated employment, and encouraged capital formation along the way. The Bank remains committed to advancing financial inclusion through its expansion programmes, bringing its products and services to the rural populace in every corner of the island.

The Bank is committed to developing the communities it operates in. In addition to financial services, the Bank provides value added services for emerging communities, including training and development programmes for entrepreneurs and SMEs.

Beyond traditional brick and mortar structures, the Bank embraces technology to provide its customers with greater accessibility to its products and services, and greater convenience through products such as the DFCC Virtual Wallet.

Province	GDP (LKR million) 2015 (b)	Provincial % of Total GDP	DFCC Bank Branches	Bank's Provincial Presence (%)	Rank Based on Total GDP
Western	4,357,581	41.2	38	27.54	1
Central	1,152,391	10.3	18	12.32	3
Southern	1,159,693	10.4	21	15.23	2
North Western	1,223,830	10.9	12	8.69	5
Eastern	670,760	6.0	10	7.25	6
Sabaragamuwa	781,112	7.0	16	11.59	4
North Central	607,118	5.4	9	6.52	7
Uva	587,118	5.2	9	6.52	8
Northern	390,689	3.5	6	4.34	9

(b) Provincial
Source – adapted from Central Bank of Sri Lanka

Strategic CSR

DFCC Bank's Corporate Social Responsibility (CSR) is based on a 4E strategy covering Entrepreneurship, Environment, Emergency Relief, and Education. This holistic approach is inspired by the Bank's brand values, strengths, and processes.

Schemes Launched Under Strategic CSR During the Year

"Samata English" Pilot CSR Project

DFCC Bank firmly believes in the positive impact that education can have on children, and the lasting impact it can leave on the nation. Hence, the Bank considers education to be a key pillar of its CSR initiatives. In line with this, DFCC Bank has actively supported education in the country through various initiatives over the years.

During the year, as a part of its commitment to uplifting the standards of education in the country, the Bank initiated a pilot English education programme, "*Samata* English", in the Gampaha and Kalutara areas, aimed at enhancing competency in English among youth aged 16-22 and equipping them with the basic English knowledge required to enter the workforce. The Bank tied up with Winner International, an institution specialising in teaching Spoken English to youth for this purpose.

The Spoken English course was conducted at DFCC's Gampaha and Kalutara branches from April to August 2017, with approximately 45 youth participating. The initiative had a satisfactory outcome, and the Bank plans to expand the initiative to other areas across the country in the near future.

Community-based CSR Initiatives

CSR by DFCC REDS

During the year, the DFCC REDS organised school supplies to assist children from under privileged backgrounds, partially funded by staff contributions.

Disaster Relief Initiatives

The Bank participated in disaster relief efforts for significant segments of the community who were impacted by the inclement weather.

The Bank, along with the employees, generously donated funds to assist impacted colleagues and the larger community. Employees also contributed their time and effort to prepare ration packs for victims, and assisted at medical camps organised by the Bank in Akuressa and Deniyaya.

Flood Relief Programme

Helping Hand to Schools Affected by Floods

Having identified the needs of six schools affected by the May 2017 floods, DFCC Bank provided necessary school items for students at Mihindu Vidyalaya in Ratnapura, Gamini Central College, Kalawana, and Lankagama Junior Model School in Lankagama, off Deniyaya. The Bank also donated Duplo machines to Matara Primary Model School and Weragampitiya Olcott Model School, and 300 chairs to Diyagama Vidyalaya in Kalutara.

Eye Donation Campaign

DFCC Bank became the first bank in Sri Lanka to partner with the National Eye Bank (NEB) in conducting a successful Eye Donation Campaign, which resulted in 300 donors comprising DFCC employees and the general public donating their eyes towards the cause of alleviating corneal blindness.

Scholarship Seminar

Special workshops were conducted for Grade five Scholarship students and their parents by specialist lecturers who shared knowledge on preparing children for the exam, parenting tips and more. The seminars were conducted under the strict supervision of past teachers/principals' associations. These seminars were held in Gampaha, Kurunegala, Kandy, Tangalle, Anuradhapura, Bandarawela, Matara, Dambulla, and Kaduruwela.

Sponsorships

DFCC Bank often sponsors selected events across the country that appeal to various target segments. Sponsorships are verified based on internal policies of eligibility, transparency, and due process. The following are some of the significant initiatives that DFCC Bank supported during the period under consideration:

Strategic Partner of the Colombo International Tea Convention

As part of its ongoing commitment to the country's business community, DFCC Bank supported the Colombo International Tea Convention held in August 2017 as "Strategic Partner". Marking 150 years of the Ceylon Tea Industry, the Colombo Tea Traders Association organised the event which attracted over 100 foreign delegates, over 500 local participants, and high level dignitaries and Government officials. By partnering with such key events, DFCC Bank created value and growth opportunities for customers in the Tea Industry.

The Bank highlighted its comprehensive range of financial solutions aimed at the tea industry during the convention. Together with its IT subsidiary; Synapsys, the Bank presented its revolutionary supplier settlement system. The system supports Sri Lanka's well-established community of private tea manufacturers and tea leaf suppliers by enabling suppliers to have revenue from their sales managed by a bank and be transferred directly into their bank account.

Gold Sponsor of the Sinhala and Tamil New Year Celebrations of the Sri Lankan Coordinating Committee Qatar (SLCC)

DFCC Bank was the Gold Sponsor of the 2017 Sinhala and Tamil New Year Celebrations organised by the Embassy of Sri Lanka in collaboration with the Sri Lanka Coordinating Committee Qatar. The event had a line-up of many traditional and sports events with the participation of community members.

Official Banking Partner for Gajaba Super Cross 2017

DFCC Bank was the official banking partner for the *Gajaba* Super Cross 2017, an annual racing championship held by the Gajaba Regiment of the Sri Lanka Army in collaboration with the Sri Lanka Autosports Drivers Association (SLADA). The event celebrated its 16th successive year in 2017 at the Supercross track in Saliyapura, Anuradhapura.

Joint Title Sponsorship of the 2017 Inter-School Golf Tournament

DFCC Bank has been a proud sponsor of sporting events in Sri Lanka. The Bank believes that sports brings people together, to work and grow together – core beliefs in DFCC Bank's own philosophy for growth.

DFCC Bank was the Joint Title Sponsor of the 2017 Inter-School Golf Tournament, conducted by the Royal Colombo Golf Club (RCGC). Held in December 2017 at the Royal Colombo Golf Club for the fourth consecutive year, the Tournament featured over 250 Golfers from over 25 of the country's top schools, including five girls schools.

Environment Capital

Managing resources

DFCC Bank adopts the 3R concept – Reduce, Reuse, Recycle – when procuring and managing resources. The Bank periodically review its resource consumption and look at innovative methods of conserving energy and providing business solutions in a proactive manner.

Waste Management Projects

Promoting Reusable Bags through a Paper-Recycling Project

DFCC Bank's Community Projects team collaborated with the Sustainability Unit to launch a DFCC-branded reusable bag for staff members – a first in the banking industry. By encouraging the "Take Your Own Bag (TYOB)" concept among staff, the Bank expects to reduce the use of polythene bags by one million per year.

In light of the garbage crisis facing Colombo city and suburbs, this initiative engages staff in making a direct contribution to resolving the problem of garbage disposal. The initiative was partly funded by proceeds received from a paper recycling week conducted by the Community Projects team across the entire branch network of the Bank.

e-waste Drive 2017

Initiated by the Sustainability Unit, the e-waste collection and disposal initiative encouraged staff members to bring their e-waste and put them in a designated bin, which was then collected by an approved e-waste recycling company. The initiative engaged DFCC Bank staff to participate in a sustainable activity, making a direct contribution to resolving the problem of garbage disposal.

GHG Emissions

DFCC Bank is reporting its greenhouse gas (GHG) emissions on a voluntary basis for the sixth consecutive year. The physical boundary remains the same as in the previous years which is "DFCC Banking Business".

As before, the calculations are based on the WBCSD/WRI Greenhouse Gas Protocol Corporate Standard and the most recent versions of applicable calculation tools. The reporting under ScopWe 1 and Scope 2 is complete except for fugitive emissions from air conditioning plants, which are relatively insignificant. Reporting on Scope 3, which is optional, is selective based on significance and data availability.

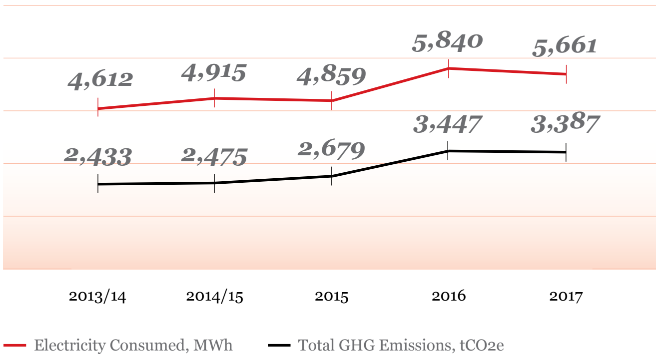
Carbon Footprint

Scope	Source	GHG emissions			
		2017		2016	
		tCO_2e	%	tCO_2e	%
Scope1 (direct)	Stationary combustion	**5.22**	**0.15**	38.1	1.1
	Mobile combustion	**172.8**	**5.1**	117.3	3.4
	Total scope 1	**178.01**	**5.26**	155.4	4.5
Scope 2 (indirect)	Purchased electricity (CEB)	**1,040.4**	**30.71**	1,032.3	30.0
	Total scopes 1 and 2	**1,218.40**	**35.97**	1,187.6	34.5
Scope 3 (indirect)	Stationary combustion	**91.27**	**2.69**	102.4	3.0
	Purchased electricity (CEB)	**2,028.08**	**59.87**	2,132.8	61.9
	Employee air travel	**49.69**	**1.47**	24.0	0.7
	Total scope 3	**2,169.04**	**64.03**	2,259.1	65.5
	Total scopes 1, 2 and 3	**3,387.44**	**100.0**	3,446.8	100.0

Note: Totals may not tally exactly due to rounding

The total GHG emissions during the period under review amounted to 3,387 tonnes carbon dioxide equivalent (tCO_2e), a decrease of 1.72% over the previous year.

Managing Environmental Impact



Indirect GHG emissions from purchased electricity was by far the single largest contributor, accounting for 30.71% of the total in respect of Bank-owned premises (2016: 30%) and another 59.87% of the total in respect of rented premises (2016: 62%), bringing its total share to 90.58% (2016: 92%).

Given the nature of business, the relatively high proportion of electricity in our total GHG emissions is to be expected.

Environmental Friendly Initiatives

Tree Planting Campaigns Commemorating Staff Birthdays

In line with its long-term sustainability initiatives and the "Great Place to Work" programme, DFCC Bank, through the Sustainability Unit, launched a commemorative staff tree-planting campaign in 2017. The campaign saw the Sustainability Unit planting trees on a monthly basis to celebrate every staff member's birthday. Staff members are sent personalised invitations to attend the tree-planting campaign with their families, and given an e-tree-dedication certificate with a Google Maps link of the exact location of the tree.

During 2017, 11 tree planting campaigns took place in areas such as Aranayake, Kaduwela, Jaffna, Duplication Road, Thalawila, Athurugiriya, Kahathuduwa, Beddagana, Bellanwila, and Batticaloa. 7,355 trees were planted, with approximately 1,700 trees planted to commemorate staff birthdays. Some campaigns were carried out with

11

tree planting campaigns with 7,355 trees planted

Winner of the Merit Award for

Outstanding Business Sustainability Achievement

at Karlsruhe Sustainable Finance Awards 2017

Winner in the

SME Development

category at ADFIAP Development Awards 2017

"Reforest Sri Lanka", a voluntary organisation committed to building a better environment.

Many endemic and native species, such as *Mee, Kumbuk, Karanda, Gammalu, Kos*/Jack Fruit, V*eera, Ehala, Rath Handun, Sudu Handun, Hora, Ranawara, Atamba, Wara,* and *Olinda* were planted during these campaigns. The trees planted under this initiative will help to reforest key areas across the island, help to improve soil quality and minimise soil erosion.

The campaigns were well attended by staff members and their families, including senior management, and members of the local community. The commitment and support of the Bank's top management, including the Chairman, Board of Directors, CEO, and Deputy CEO were a key success factor for the initiative. The hope is that the initiative instills in staff and their families, a greater commitment towards protecting the planet and operating as responsible corporate citizens.

Beach Clean-up

The DFCC Community Projects team held their first Beach Clean-up Day on 19 August at the Mount Lavinia Beach. Situated close to Colombo, the beach is one of the most polluted areas, littered with plastic bottles, polythene, glass, fishnets, and other refuse. Over 80 large garbage bags were filled by a large number of DFCC staff, including CEO Mr Lakshman Silva, and their families, who volunteered their time to help out on the day, together with locals.

Celebrating World Earth Hour 2017

Earth Hour is a global event organised by the World Wildlife Fund. DFCC Bank supports this initiative by switching off all signboard lights across all its branches, serving as an example to the wider community to adopt a more responsible attitude towards the environment. The Bank raises awareness on climate change by requesting staff to turn-off all non-essential lighting and electrical appliances during the World Earth Hour in their households.

Establishment of a Social and Environmental Management System (SEMS)

The Bank recognises the impact economic development can have on the environment and social aspects of life. Therefore, the Bank places high importance on environmental and social appraisal when making investment-decisions and managing internal operations.

To this extent, the Bank has established the Social and Environmental Management System (SEMS), as implemented by the Sustainability Unit. SEMS ensures that the performance of existing operations and environmental/social implications due to existing/proposed projects are reviewed, and subsequent monitoring is carried out to maintain stipulated environmental standards.

Playing an Active Role in the Sustainable Banking Initiative

The Sri Lanka Sustainable Banking Initiative (SBI) is promoted by the Sri Lanka Banks Association (SLBA) and funded by DEG of Germany, OeEB of Austria, Proparco of France, and FMO of Netherlands. In November 2015, DFCC Bank joined 17 other banks in Sri Lanka for signing up for 11 Sustainable Banking Principles for Sri Lanka, under Phase I of the initiative.

Commenced in August 2017, Phase II of the initiative will provide guidance documents, training, coaching, E-learning, and case studies over a period of 18 months. DFCC Bank plays an active role in the SBI, with its Assistant Vice President for Sustainability being a member of the core team, which was formed to take Phase II forward.

Winning Sustainability Awards

DFCC Bank was awarded a Merit Award for "Outstanding Business Sustainability Achievement" at the Karlsruhe Sustainable Finance Awards in July 2017, in recognition of its success in incorporating sustainability in its corporate strategy and its business processes.

DFCC Bank was a winner in the "SME Development" category for setting up a specialised unit for development of MSMEs at the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP) Development Awards, held in May 2017 in Macau, China.

...and exceeding expectations of the times.

There was a time when banks were only expected to provide financial solutions. Today, banks are expected to go beyond and provide business solutions. DFCC provides financial and IT consultancy services through the subsidiary companies – DFCC Consulting (Pvt) Limited and Synapsys Limited.

Awards and Accolades

Category	Awards	Project	Institution	Month
SME Development	Winner	Setting up a specialised unit for development of MSMEs	Association of Development Financing Institutions in Asia and the Pacific (ADFIAP)	May 2017
Best Common ATM Acquirer of the Year (Category C) and Bank of the Year for Financial Inclusivity (Category C)	Merit	Use of the country's national payment infrastructure and innovative technology to promote digital transactions	Lanka Pay, Techinnovation Awards 2017	June 2017
Outstanding Business Sustainability Achievement award	Merit	DFCC Bank's sustainability initiatives	Global Sustainable Finance Conference, City of Karlsruhe, Germany	July 2017
Business Today Top 30	Position 21	Corporate	Business Today Magazine	November 2017
Special award	Best Annual Report	DFCC Bank Annual Report 2016	Association of Development Financing Institutions in Asia and the Pacific (ADFIAP)	December 2017
Human Capital Development	Plaque of Merit	Building a Cohesive Value-Based Internal Culture	Association of Development Financing Institutions in Asia and the Pacific (ADFIAP)	December 2017

Integrated Risk Management

Risk Culture and Vision

DFCC Bank PLC (Bank) adopts a comprehensive and well-structured mechanism for assessing, quantifying and managing risk exposures which are material and relevant for its operations within a well-defined risk framework. The articulated set of limits under the risk management framework explains the risk appetite of the Bank for all material and relevant risk categories and the risk capital position. Risk management is integrated with strategic, business and financial planning and customer/client transactions, so that business and risk management goals and responsibilities are aligned across the organisation. Risk is managed in a systematic manner by focusing on a group basis as well as managing risk across the enterprise, individual business units, products, services, transactions, and across all geographic locations.

The following broad risk categories are in focus:

- Business risk and strategic risk
- Credit risk including settlement risk in Treasury and international operations and credit concentration risk
- Interest rate risk in the banking book and the trading book
- Liquidity risk
- Foreign currency risk
- Equity prices risk
- Operational risk
- Legal risk
- Compliance risk
- Reputational risk
- Country risk
- Information systems security risk

Credit risk amounts to the highest quantum of quantifiable risk faced by the Bank based on the currently effective quantification techniques. DFCC Bank's credit risk accounted for 91% of risk-weighted assets. Additionally, the Bank takes necessary measures to proactively manage operational and market risks as very important risk categories considered as Pillar I risks under the Basel regulations. Operational risk incidents may be with high frequency but low impact or with low frequency but high impact all of which warrant being closely monitored and managed prudently.

The Bank's general policies for risk management are outlined as follows:

a. The Board of Directors' responsibility for maintenance of a prudent integrated risk management function in the Bank.

b. Communication of the risk policies to all relevant employees of the Bank.

c. Structure of "Three Lines of Defence" in the Bank for management of risks which consists of the risk-assuming functions, independent risk management and compliance functions and the internal and external audit functions.

d. Ensuring compliance with regulatory requirements and other laws underpinning the risk management and business operations of the Bank.

e. Centralised integrated risk management function which is independent from the risk assuming functions.

f. Ensuring internal expertise, capabilities for risk management and ability to absorb unexpected losses when entering into new business, developing products, or adopting new strategies.

g. An assessment of risk exposures on an incremental and portfolio basis when designing and redesigning new products and processes before implementation. Such analyses will include among other areas, business opportunities, target customer requirements, core competencies of the Bank and the competitors and financial viability.

h. Adoption of the principle of risk-based pricing.

i. Ensuring that the Board approved target capital requirements, which are more stringent than the minimum regulatory capital requirements, are not compromised. For internal purposes, economic capital is quantified using Basel recommended guidelines in the Internal Capital Adequacy Assessment Process (ICAAP). A cushion for the regulatory capital over and above the economic capital requirement is maintained to cover for stress losses or losses caused by unquantifiable risks such as strategic risk, liquidity and reputation risk (risk categories which are not in Pillar I of Basel guidelines). Under ICAAP, capital is monitored on a quarterly basis based on certain stress scenarios which are subject to regular review based on macro-level anticipated developments.

j. Aligning risk management strategy to the Bank's business strategy.
k. Ensuring comprehensive, transparent, and objective risk disclosures to the Board, corporate management, regulators, shareholders and other stakeholders.
l. Continuous review of risk management framework and ICAAP to align with Basel recommendations and regulatory guidelines.
m. Maintenance of internal prudential risk limits based on the risk appetite of the Bank wherever relevant, over and above the required regulatory limits.
n. Ensuring a prudent risk management culture within the Bank.
o. Periodic review of risk management policies and practices to be in line with the developments in regulations, business environment and internal environment.

A risk management culture has been created across the Bank that promotes its business objectives and an environment that enables management to execute the business strategy in a more efficient and sustainable manner. The Board of Directors regularly review the risk profile of the Bank and its Group, and every business or function is included in developing a strong risk culture within the Bank. Further, the Bank ensures that, every employee has a clear understanding of their responsibilities in terms of risks undertaken by them in every step they take in their regular business activities. This has been inculcated mainly through the Code of Conduct, periodically conducted training programmes, clearly defined procedural manuals and Integrated Risk Management function's involvement as a review process in business operations.

Risk Governance

Approach of "Three Lines of Defence"

DFCC Bank PLC advocates strong risk governance applied pragmatically and consistently with a strong emphasis on the concept of "Three Lines of Defence". The governance structure encompasses accountability, responsibility, independence, reporting, communication and transparency, both internally and with our relevant external stakeholders.

The First Line of Defence involves the supervision and monitoring of risk management practices by the business managers, corporate management and executive committees while discharging their responsibilities and accountability for day-to-day management of business operations. Independent risk monitoring, validation, policy review and compliance by the Integrated Risk Management Department (IRMD), the compliance function and periodic monitoring and oversight by the Board Integrated Risk Management Committee (BIRMC) constitute the Second Line of Defence. The Third Line of Defence is provided by the independent check and quality assurance of the internal and external audit functions.

Risk governance of the Bank includes setting and defining the risk appetite statement, risk limits, risk management functions, capital planning, risk management policies, risk infrastructure, MIS and analysis to monitor the Bank's risk profile. The Bank exhibits an established risk management culture with effective risk management approaches, systems and controls. Policy manuals, internal controls, segregation of duties, clearly demarcated authority limits and internal audit form a part of key risk management tools. The Bank has developed a risk management framework covering risk governance, which includes, risk management structure comprising different subcommittees and clearly defined reporting lines ensuring risk management unit is functioning independently. The Group Chief Risk Officer (CRO), who is an Executive Vice President functions with direct access to the BIRMC.

Governance Structure for Risk Management at DFCC Bank PLC

The Concept of "Three Lines of Defence" for Integrated Risk Management Function of DFCC Bank PLC

First Line of Defence	Second Line of Defence	Third Line of Defence
Involvement by the Board, CEO, Deputy CEO, Senior Management Committees. Accountability and responsibility of senior and middle management supported by internal controls, governance structure, processes and risk management.	*Oversight by the BIRMC and independent risk monitoring, and compliance by IRM, Compliance and General Legal.*	*Oversight by the Board's Audit Committee, and independent check and quality assurance.*
Strategy, Performance and Risk Management	**Policy, Monitoring and Oversight**	**Independent Assurance**
Board of Directors and Board Committees Chief Executive Officer and Management Committees Corporate Banking; Branch Banking; Business Banking; Treasury General Operations; HR; Rehabilitation and Recoveries; IT; Litigation Unit International Operations; Consumer Banking; Credit Administration; Branch Credit Management Bancassurance; Business Legal; Marketing; Planning; NSC	Compliance and General Legal Integrated Risk Management	Internal Audit External Audit

Risk Policies and Guidelines

A set of structured policies and frameworks approved by the BIRMC and the Board forms a key part of the risk governance structure. Integrated Risk Management Framework stipulates, in a broader aspect, the policies, guidelines, and organisational structure for the management of overall risk exposures of the Bank in an integrated approach. This framework defines risk integration and the aggregation approaches for different risk categories. In addition, separate policy frameworks detail the practices for management of key specific risk categories such as credit risk, market risk, credit concentration risk, liquidity risk, and operational risk. These policy frameworks are reviewed annually and communicated across the Bank.

Respective staff members are required to adhere to the specifications of these frameworks when conducting business transactions.

Risk Appetite

Risk appetite of the Bank has been defined in the Overall Risk Limits System. It consists of risk limits arising from regulatory requirements, borrowing covenants and internal limits for prudential purposes. The Limits System forms a key part of the risk indicators and covers key risk areas such as credit, interest rate, liquidity, operational, foreign exchange, concentration, and risk capital position amongst others. Lending limits cover the industry sectors and geographical regions as part of the prudential internal limits. Industry sector limits for the lending portfolio considers the inherent diversification within the subsectors and the borrowers within broader sectors. These limits are monitored monthly and quarterly on a "Traffic Light" system. These risk appetite limits are reviewed at least annually in line with the risk management capacities, business opportunities, business strategy of the Bank and regulatory specifications.

In the event the risk appetite threshold has been breached or it is approaching the levels not desirable by the Bank, risk management measures and business controls are implemented to bring the exposure level back within the accepted range. Risk appetite, therefore, translates into operational measures such as new or enhanced limits or qualitative checks for the dimensions such as capital, earnings volatility and concentration of risks.

Tolerance Limits for Key Types of Risks

Risk Area	Risk Appetite-Criteria	Limit/Range
Integrated Risk and Capital management	Total Tier I Capital Adequacy Ratio (under Basel III) (Total Tier I capital as a percentage of total risk-weighted assets)	7.25% (2017) – 7.875% (2018)
	Total Capital Adequacy Ratio (under Basel III) (Total capital as a percentage of total risk-weighted assets)	11.25% (2017) – 11.875% (2018)
Credit Quality and Concentration	NP Ratio	5% (Internal)
	Single Borrower Limit – Individual	30% (Regulatory)
	Single Borrower Limit – Group	33% (Regulatory)
	Aggregate Large Accommodation	55% (Regulatory) 45% (Internal)
	Exposures to Industry Sectors	5% to 20% (Internal)
	Aggregate Limit for Related Parties	25% (Internal)
Liquidity Risk	Liquid Asset Ratio for DBU and FCBU	20% (Regulatory)
	Liquidity Coverage Ratio (All Currencies and Rupee only)	80% (2017) – 90% (2018)
Market Risk	Forex Net Open Long Position/Short Position	USD 3 – 18 million
Operational Risk	Reputation risk of the Bank	Zero or very low risk appetite
	Operational risks due to internal and external frauds, employee practices and workplace safety, client products and business practices, damage to physical assets, business disruption and systems failures and failures in execution, delivery and process management	

Board Integrated Risk Management Committee (BIRMC)

The BIRMC is a Board subcommittee, which oversees the risk management function and the provisions of Basel III implementation as required by the Regulator from time to time in line with Board-approved policies and strategies. The BIRMC functions under the responsibilities set out in the Board-approved Charter for the BIRMC, which incorporates corporate governance requirements for Licensed Commercial Banks issued by the Central Bank of Sri Lanka (CBSL). BIRMC sets the policies for bank-wide risk management including credit risk, market risk, operational risk and liquidity risk. In addition to the Board representatives, the BIRMC consists of the CEO and CRO as members. Further, Heads representing Credit, Finance, Treasury, Information Technology, Operations and Compliance attend the meeting as invitees. A summary of the responsibilities and functions of the BIRMC is given in the Report on the Board Integrated Risk Management Committee on page 136 of this Annual Report.

The BIRMC meets at least on a quarterly basis and reviews the risk information and exposures as reported by the Integrated Risk Management Department, Treasury, Finance and the other business and service units. Risk reporting includes reports on overall risk analysis relating to the Bank's capital, risk appetite, limits position, stress testing, any strategic risks faced by the Bank and risk analysis of the Group companies. Additionally, they include reports covering the main risk areas such as credit risk, market risk and liquidity risk, operational risk, information systems security risk and compliance risk.

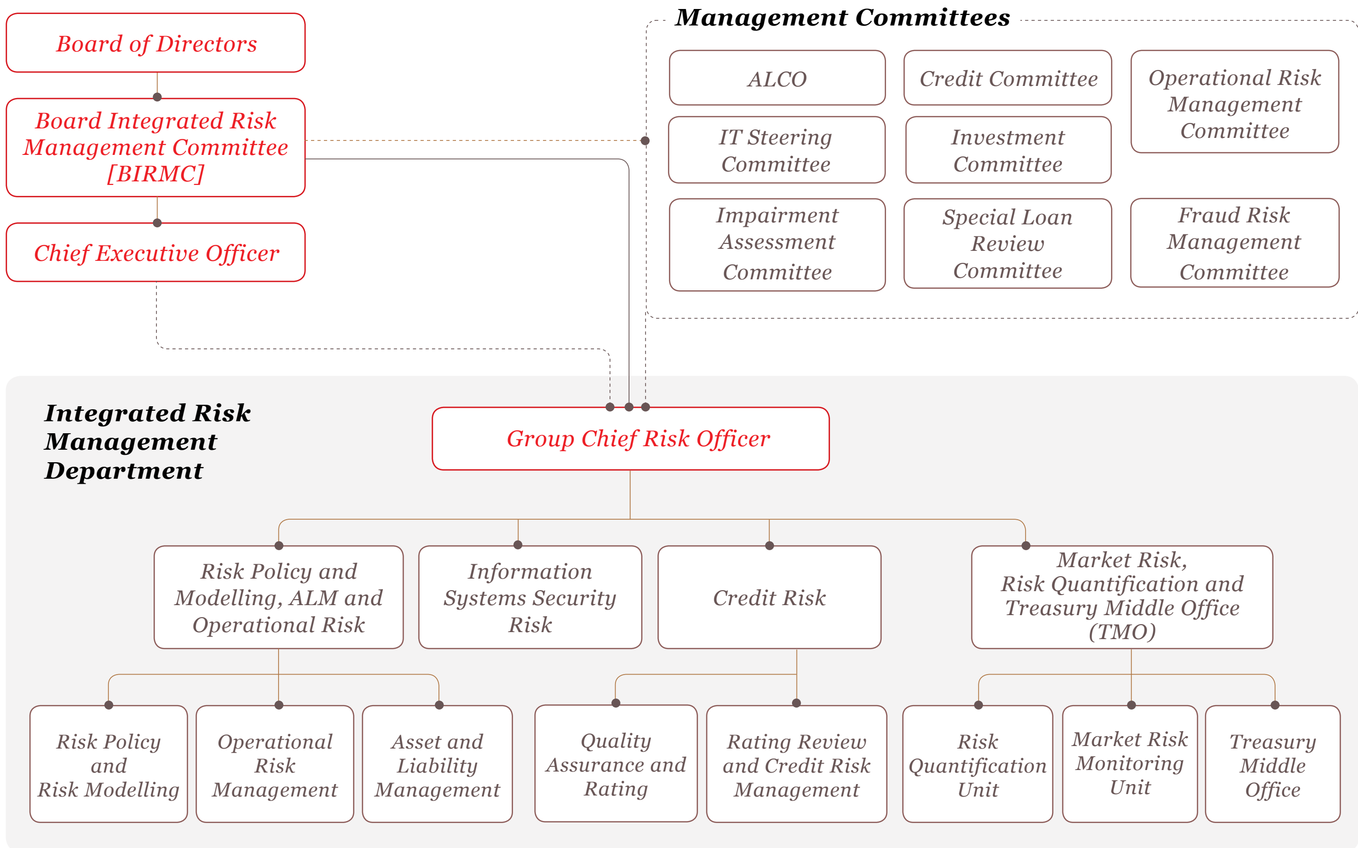
Scope and Main Content of Risk Reporting to Board and Senior Management

Risk Type	Scope and Main Content of Risk Reporting
Overall Risk	→ Review of the Internal Capital Adequacy Assessment Process (ICAAP) → Regulatory Capital Adequacy position and trends compared with limits → Overall risk limit system including regulatory and advisory/internal limits → Stress testing of key risks and overall exposures → Reports on top and emerging strategic and business risks → Risk analysis of Group companies → Risk analysis of new products and changes to products
Credit Risk	→ Credit portfolio analysis and risk quantifications → Analysis of concentration of the lending portfolio (HHI computation) → Summary of Loan Review Mechanism → Reports on validation results and changes implemented for risk rating models
Market and Liquidity Risk	→ Reports on liquidity and foreign exchange risk management by Treasury → Market risk analysis by Treasury Middle Office and review of any limits → Equity portfolio analysis → Liquidity risk monitoring under stock and flow approaches → Status report of margin trading facilities → Analysis of investment, trading and fixed income trading portfolio → Report of key decisions and recommendations by ALCO
Operational Risk	→ Key decisions and recommendations by the Operational Risk Management Committee (ORMC) → Reports on Business Continuity Plan and disaster recovery drills undertaken
IT and systems security Risk	→ External vulnerability assessment reports → Information security policies and status of implementation → Reports of the ORMC on information security → Status of information systems security plan
Compliance Risk	→ Status of the Bank's compliance with rules and regulations → Report on new rules and regulations → Review of compliance related policies and procedures

Involvement of Management Committees

Management Committees such as the Credit Committee (CC), Asset and Liability Management Committee (ALCO), Operational Risk Management Committee (ORMC), Fraud Risk Management Committee (FRMC), Special Loan Review Committee (SLRC) and Impairment Assessment Committee (IAC) are included in the organisational structure for integrated risk management function. The responsibilities and tasks of these Committees are stipulated in the Board-approved Charters and Terms of Reference (TOR) and the membership of each committee is defined to bring an optimal balance between business and risk management.

Organisational Structure for Integrated Risk Management



The Integrated Risk Management Department (IRMD) is responsible for measuring and monitoring risk at operational levels on an ongoing basis to ensure compliance with the parameters set out by the Board/BIRMC and other Executive Committees for carrying out the overall risk management function in the Bank. It consists of separate units such as Risk Policy and Modelling, Credit Risk Management and Quality Assurance, Market Risk Monitoring, Operational Risk Management, Risk Quantification, Information Systems Security Risk Monitoring and Treasury Middle Office. IRMD is involved with product or business strategy development or entering into new business lines and gives input from the initial design stage throughout the process from a risk management perspective.

Key Developments in Risk Management Function During the Period Under Review

Several significant initiatives were undertaken focusing continuously on regulatory developments and reassessing the Bank's existing risk management policies, guidelines and practices for necessary improvements. The improvements brought in by adopting the Basel III Regulatory Standards by the banks in Sri Lanka from mid 2017 is crucial. In addition to these regulatory specifications, changes in business strategy, industry factors and international best practices were also considered in the improvement process. The following are the key initiatives during the period under review which led to further improvements in the overall integrated risk management function.

Prudential risk limits were reviewed in order to reflect the current risk appetite of the Bank by setting new limits wherever necessary. The Bank set new milestones to improve the advances to Deposits Ratio and Current and Savings Accounts (CASA) Ratio and targets were set in order to maintain adequate Liquid Asset Ratios. New limits were set for liquidity and foreign exchange risks in order to manage deposit concentration and the increasing swap cost of the Bank respectively. Further, based on the current risk appetite, the Bank introduced a new exposure limit for lending to Maldives to manage the country concentration risk.

All the Board-approved risk management frameworks, charters, and TORs were reviewed during the period, especially considering the changes in new regulations and the Bank's business model.

Periodic validation of the credit rating models was carried out for better discriminatory power, while new scorecards were introduced for retail lending. As part of establishing an independent model validation process, the Bank has engaged the services of a foreign risk management consultancy firm to obtain an independent validation for its corporate banking and leasing rating models and certain recommended improvements have been incorporated for the corporate rating model. Additionally, development of new scorecards are in progress for new business areas the Bank intends to focus more on such as credit cards and Micro Small and Medium Enterprise lending. A new two dimensional scorecard catering to all types of personal financial services was deployed during the year, which replaced the stand-alone models previously used.

Treasury Middle Office (TMO) which is functionally segregated from the Treasury Department, directly reports to the Group CRO and monitors the Treasury-related market risk limits. The TMO uses a dashboard that facilitates the timely reporting of Treasury market positions independently to the Management. TMO jointly with Treasury has embarked on a new Treasury system implementation project expected to be deployed by mid 2018, which would increase the efficiency of Treasury operations and risk management by TMO, while automating the TMO dashboard.

During the years in the recent past, the interest margins came under pressure with the sharp drop in the market rates, where lending rates dropped faster than the deposit rates. Scenario analysis and simulations by the ALM unit to assess the expected behaviour of interest margins enabled ALCO to take proactive measures to manage the erosion of margins. Looking at the trends in the market rates, ALCO proactively changed the pricing methods, thus enhancing the net interest margins of the Bank in late 2016 continuing to 2017. The Bank, being net asset sensitive to interest rate changes in the shorter term was able to improve the interest margins with the increase in the market rates.

IRMD continued to calculate loss ratios for key lending products using historical recovery data in support of impairment assessment under IFRS. IRMD continued to support the pawning business of the Bank through timely studies, research and providing necessary market information to the business. IRMD was actively engaged in arriving at advance rates and interest rates for pawning products while managing the market and credit risk aspects.

As part of the risk management practices, the Bank computed the key credit risk quantification parameters such as Probability of Default (PD), Loss Given Default (LGD) and the loss ratios which are defined and recommended under the Basel III and IFRS. The results indicated improvements in the credit risk rating process, rating models, recovery process and the collateral quality in the Bank.

The credit workflow of the Bank was further improved during the year with the absorption of the Quality Assurance Unit under IRMD from the latter part of 2016. The new workflow ensures that every credit proposal except for centrally processed retail loans, is evaluated by an independent authority not connected to business lines, being either the Credit Risk Management Unit (CRMU) or the Quality Assurance Unit (QAU) of IRMD, based on the size of the accommodation and the approving authority.

The stress testing framework was strengthened during the year to include stress testing in relation to the economic and macro environmental factors.

Having duly recognised the global trend on increasing threats on systems and information security, the Bank increased its focus on IT systems security under its operational risk management practices. The scope of the Information Security Monitoring Unit was further improved during the year under the Integrated Risk Management Department to proactively manage the information security risk of the Bank. Staff awareness programmes on operational risk were held across the Bank on a regional basis especially for the newly appointed Operational Risk Coordinating Officers (ORCOs) while assigning specific reporting responsibilities to them. The Bank has developed a model for Risk and Control Self-Assessment, and Key Risk

Indicators for operational risks across all major functions and departments, and continues to monitor closely their applicability, trends and adequacy of the necessary controls to be in place. The Operational Risk Management Committee oversees the effectiveness of security initiatives and directs the management of information security risks within the Bank.

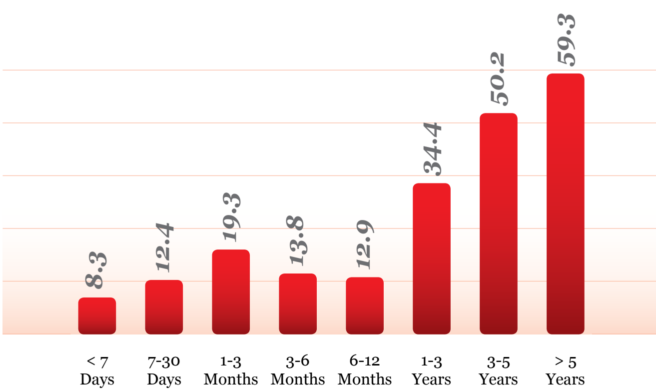
DFCC Bank PLC developed a Fraud Risk Management Policy with the objective of identifying any potential frauds and to take necessary mitigating measures and creating awareness among the employees to establish a corporate culture and to create an environment that inhibits fraud. As part of this Policy, a Fraud Risk Management Committee was formed and will be in operation to deal with any investigations or potential frauds that could take place on a timely basis.

Credit Risk

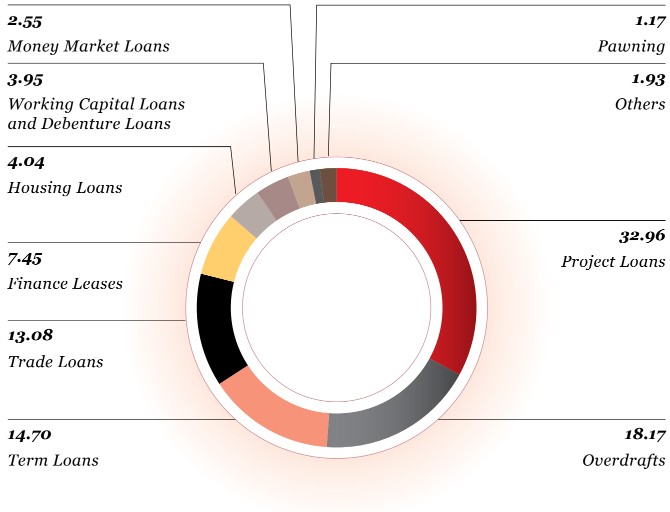
Credit risk is the risk of loss to the Bank if a customer or counterparty fails to meet its financial obligations in accordance with agreed terms and conditions. It arises principally from On-Balance Sheet lending such as loans, leases, trade finance and overdrafts as well as through Off-Balance Sheet products such as guarantees and Letters of Credit. A deterioration of counterparty credit quality can lead to potential credit-related losses for a bank. Credit risk is the largest component of the quantified risk accounting for 91% of Risk-Weighted Assets of DFCC Bank PLC.

The challenge of credit risk management is to maximise the risk adjusted rate of return by maintaining the credit risk exposure within acceptable levels.

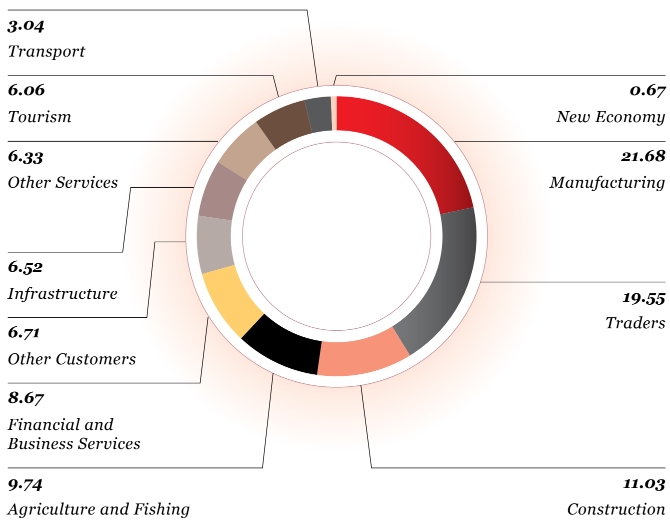
Residual Maturity of Total Advances – *LKR billion*



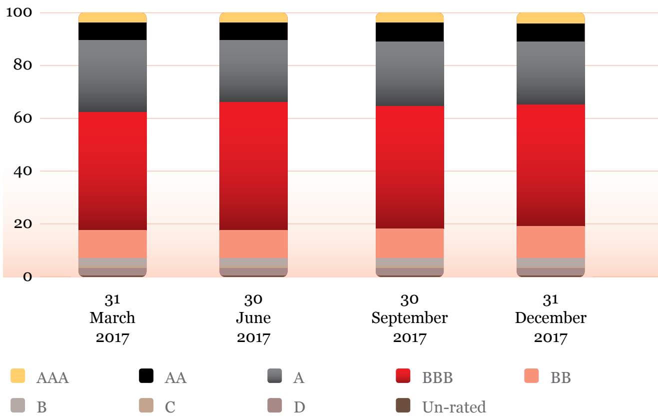
Product Composition – *%*



Sector-wise Portfolio Distribution – *%*

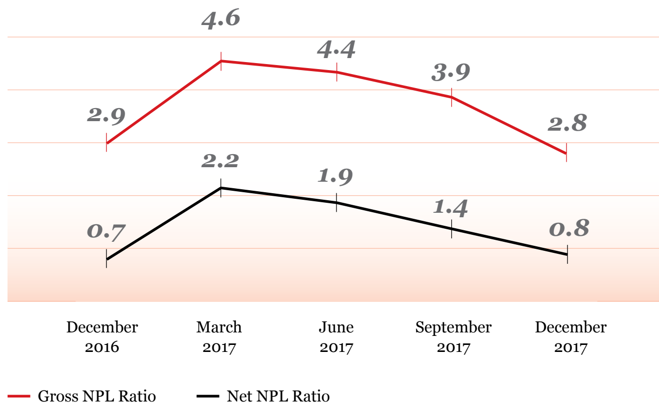


Rating Distribution of Portfolio – %

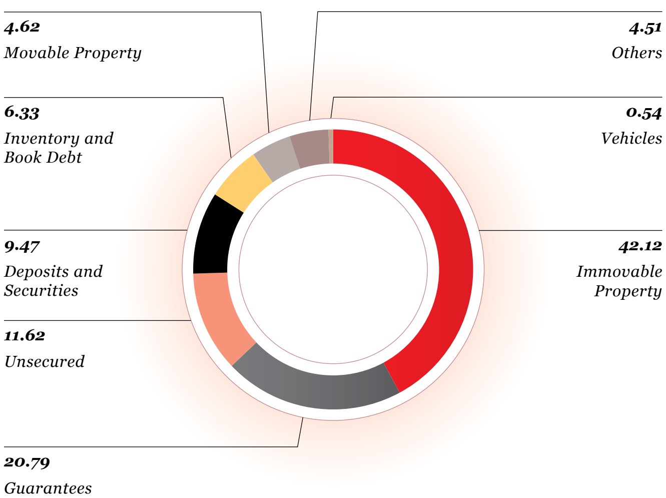


***Note:** Excludes concessionary staff loans and credit card instalment loans*

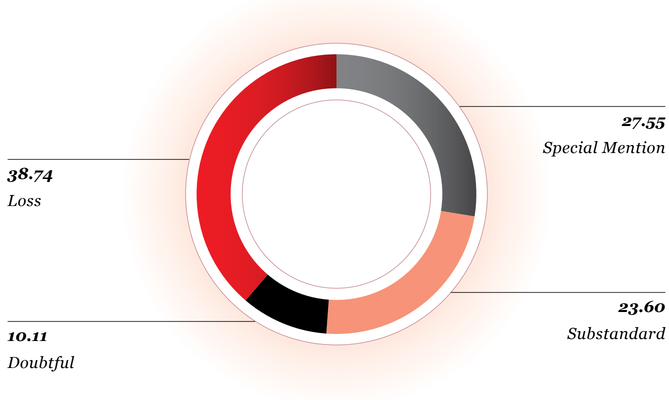
Movement of NPL – %



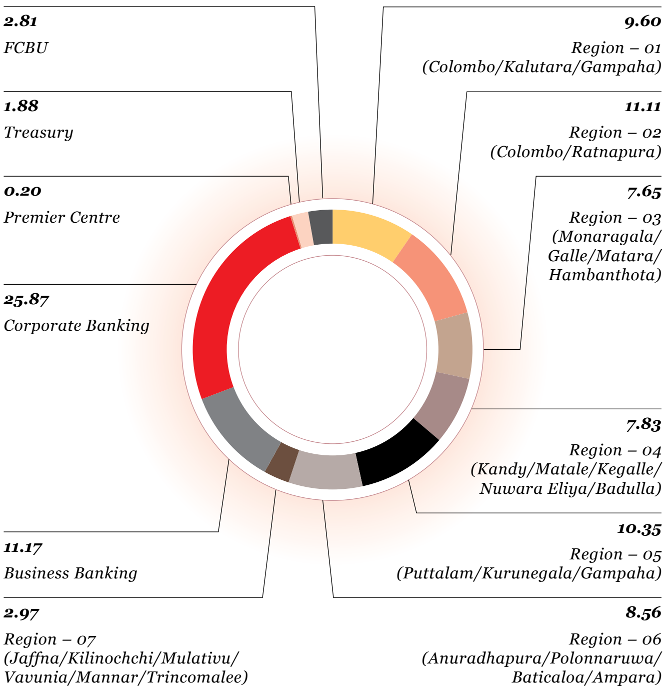
Collateral-wise Distribution of the Loans and OD Portfolio – %



NPL Composition – %



Geographical Distribution of Gross Loans and Receivables – %



Credit Risk Management Process at DFCC Bank PLC

The Bank's credit policies approved by the Board of Directors define the credit objectives, outlining the credit strategy to be adopted at the Bank. The policies are based on CBSL Directions on integrated risk management, Basel recommendations, business practices, and risk appetite of the Bank.

Credit risk management guidelines identify target markets and industry sectors, define risk tolerance limits and recommend control measures to manage concentration risk. Standardised formats and clearly documented processes and procedures ensure uniformity of practices across the Bank.

Credit Risk Culture	→ Credit Risk Management Framework and Credit Policy → Governance structure and specific organisational structure for credit risk management → IRMD creates awareness of credit risk management through training programmes and experience sharing sessions
Credit Approval Process	→ Structured and standardised credit approval process as documented in the credit manual. The entire gamut of activities involving credit appraisal, documentation, funds disbursement, monitoring performance, restructuring and recovery procedures are described in detail in the manual which is reviewed annually → Standardised appraisal formats have been designed for each product type → Clearly defined credit workflow ensures segregation of duties among credit originators, independent review and approval authority → Delegation of Lending Authority sets out approval limits based on a combination of risk levels, as defined by risk rating and security type, loan size, proposed tenure, borrower and group exposure → IRM's involvement in independent rating review of every credit proposal with the exception of centrally processed retail loans → CRO is an observer of the Credit Committee, and evaluates credit proposals from a risk perspective → Risk-based pricing is practiced at the Bank, any deviations being allowed only for funding through credit lines and where strong justification is made due to business development purposes

Control Measures	→ Negative sectors and special clearance sectors are identified based on the country's laws and regulations, the Bank's corporate values and policies and level of risk exposure. Negative sectors are recognised as industry sectors to which lending is disallowed while special clearance sectors are industry sectors and credit products to which the Bank practices caution in lending → Exposure limits on single borrower, group exposure, and advisory limits on industry sectors, large group borrowers and selected geographical regions are set by the Board of Directors on recommendation of IRMD
Credit Risk Management	→ Timely identification of problem credits through product-wise and concentration analysis in relation to industries, specific products and geographical locations such as branches/regions → Industry reports/periodical economic analysis provide direction to lending units to identify profitable business sectors to grow the Bank's portfolio and to identify industry-related risk sources and their impact → Evaluation of new products from a credit risk perspective → Post sanction review of loans within a stipulated time frame is in place in accordance with Loan Review Policy to ensure credit quality is maintained → Independent rating review by the Credit Risk Management Unit or the Quality Assurance Unit of IRMD ensures proper identification of credit quality at the time of credit origination and annual credit reviews
Credit Risk Monitoring and Reporting	→ Analysis of total portfolio in terms of NP movement, product distribution, industry sectors, Top 20 exposures, borrower rating distribution, branch-wise portfolio distribution and collateral distribution is carried out periodically and reported to BIRMC → Watch listing of clients with significant arrears and receiving feedback from regional offices on recovery action taken to regularise the position and information is disseminated to decision-makers on frequently watch-listed clients and their NP crossovers → Reporting quarterly to BIRMC on credit concentration risk positions with regard to regulatory limits such as single borrower and group exposure limits and internal advisory limits on industry sectors, large group borrowers and selected geographical regions as well as exposure based on credit rating grades → Monthly reporting on Top and Emerging Risks to BIRMC and the Board
Credit Risk Mitigation	→ Borrower's ability to pay is the primary source of recovery, whereas collateral acts as the secondary source in the event borrower's cash inflow is impaired

Key Credit Risk Measurement Tools and Reporting Frequencies

The following credit risk measurement tools are being used in managing credit risk by the Bank and reported in the stipulated frequencies:

Credit Risk Measure/Indicator	Frequency
Rating model validation results	Annually
Probability of Default	Annually
Loss Given Default (LGD) under Basel and IFRS	Quarterly/Annually
Top and emerging risks under credit risk	Monthly
Credit portfolio analysis	Quarterly
Rating-wise distribution across business segments	Quarterly
Summary of rating reviews including overridden ratings	Quarterly
Close monitoring of arrears clients	Monthly
Summary of reviews done under Loan Review Mechanism	Quarterly

Dimensions for Analysis and Monitoring of Credit Concentration Risk

Credit Risk Measure/Indicator	Frequency
Industry sector limits positions	Monthly/Quarterly
Top 20 borrower exposures	Quarterly
Top 20 borrower group exposures	Quarterly
Industry sector HHI*	Quarterly
Top 20 borrower HHI*	Quarterly
Product distribution of the credit portfolio	Quarterly
Borrower distribution across rating grades	Quarterly
Collateral concentration	Quarterly

** The Herfindahl – Hirschman Index (HHI) is a measure of concentration, calculated by squaring the share of each sector/borrower and then summing up the resulting numbers.*

Market Risk

Market risk is the possibility of losses arising from changes in the value of a financial instrument as a result of changes in market variables such as interest rates, exchange rates, equity prices, and commodity prices. As a financial intermediary, the Bank is exposed primarily to the interest rate risk and as an authorised dealer, is exposed to exchange rate risk on foreign currency portfolio positions. Market risk could impact the Bank mainly in two ways: viz, loss of cash flows or loss of economic value. Market risk can be looked at in two dimensions; as traded market risk, which is associated with the trading book and non-traded market risk, which is associated with the banking book.

The ALCO oversees the management of both the traded and the non-traded market risks. The Treasury manages the foreign exchange risk with permitted hedging mechanisms. Trends in relevant local as well as international markets are analysed and reported by IRMD and the Treasury to ALCO and BIRMC. The market risks are controlled through various limits. These limits are stipulated by the Group's Investment Policy, Treasury Manual and Overall Limits System of the Bank. Interest rate sensitivity analysis (Modified Duration analysis), Value-at-Risk (VAR), simulation and scenario analysis, stress testing and marking-to-market of the positions are used as quantification tools for the purpose risk monitoring and management of market risks.

Treasury Middle Office (TMO) is segregated from the Treasury Front Office (TFO) and Treasury Back Office (TBO) and reports to the CRO. The role of the TMO includes the day-to-day operational function of monitoring and controlling risks assumed in the TFO based on clearly defined limits and controls. Being independent of the dealers, the TMO provides an objective view on front office activities and monitors the limits. TMO has the authority to escalate limit excesses as per delegation of authority to the relevant hierarchy.

The Treasury information management system maintained by TMO includes a dashboard that facilitates the timely reporting of Treasury market positions independently to management. The strengthened Treasury and market risk management practices contribute positively to the overall risk rating of the Bank and efficiency in the overall Treasury operations. TBO which reports to the Head of Finance is responsible for accounting, processing settlements and valuations of all Treasury products and transactions. The Treasury transaction related information is independently submitted by TBO to relevant authorities.

Interest Rate Risk

Interest rate risk can be termed as the risk of loss in the net interest income (earnings perspective) or the net worth (economic value perspective) due to adverse changes in the market interest rates. Interest rate risk can consist of –

- Repricing risk, which arises from the inherent mismatch between the Bank's assets and liabilities resulting in repricing timing differences
- Basis risk, which arises from the imperfect correlation between different yield and cost benchmarks attached to repricing of assets and liabilities
- Yield curve risk, which arises from shifts in the yield curve that have a negative impact on the Bank's earnings or asset values

The Bank manages its interest rate risks primarily through asset liability repricing gap analysis, which distributes interest rate sensitive asset and liability positions into several maturity buckets. Board defined limits are in place for interest rate gaps and positions, which are monitored on a periodic basis to ensure compliance to the prescribed limits.

The Asset and Liability Management (ALM) Unit routinely assesses the Bank's asset and liability profile in terms of interest rate risk and the trends in costs and yields are reported to ALCO for necessary realignment in the asset and liability structure and the pricing mechanism. ALM performed a number of scenario analysis and simulations on the effect of interest rate changes to the Bank's interest income during the year, to facilitate pricing decisions taken at ALCO.

Foreign Exchange Rate Risk

Foreign exchange rate risk can be termed as possibility of adverse impact to the Group's capital or earnings due to fluctuations in the market exchange rates. This risk arises due to holding of assets or liabilities in foreign currencies. Net Open Position (NOP) on foreign currency indicates the level of net foreign currency exposure that has been assumed by the Bank at a point of time. This figure represents the unhedged position of the Bank in all foreign currencies. The Bank accrues foreign currency exposure through purchase and sale of foreign currency from customers in its commercial banking and international trade business and through borrowings and lendings in foreign currency.

The Bank manages the foreign exchange risk using a set of tools which includes limits for net unhedged exposures, hedging through forward contracts and hedging through creating offsetting foreign currency assets or liabilities. TMO monitors the end of the day NOP as calculated by the TBO and the NOP movement in relation to the spot movement. TMO also conducts VAR for daily forex Position and the NOP. Stress testing is also performed on a daily basis and reported by TMO. The daily inter-bank foreign currency transactions are monitored for consistency with preset limits and any excesses are reported to the management and to BIRMC.

DFCC Bank PLC has obtained approval from the Central Bank for its foreign currency borrowings and credit lines as per regulatory requirements. The unhedged foreign currency exposure of the Bank is closely monitored and necessary steps are taken to hedge in accordance with the market volatilities. In October 2013, the Bank issued a foreign currency international bond of USD 100 million with an original maturity of five years, which is to be matured in 2018 . The Bank actively manages the exchange rate arising from a minor part of this transaction where a majority has been hedged with the Central Bank. The Bank has put in place a plan after evaluating the options available for the repayment of the foreign currency bond due in 2018.

Indirect Exposures to Commodity Prices Risk – Gold Prices

The Bank's pawning portfolio amounted to LKR 2,597 million as at 31 December 2017, which was only 0.78% of total assets. The Market Risk Management Unit (MRMU) manages the risk emanating from Gold through constant analysis of the international and local market prices and adjusting the Bank's preferred Loan to Value (LTV) ratio. MRMU also conducts stress testing for the Gold portfolio by forecasting adverse Loss Given Default and PD rates. Stress results are reported to senior management via BIRMC.

Equity Prices Risk

Equity prices risk is the risk of losses in the marked-to-market equity portfolio, due to the decline in the market prices. The direct exposure to the equity price risk by the Bank arises from the trading and available-for-sale equity portfolios. Indirect exposure to equity price risk arises through the margin lending portfolio of the Bank in the event of crystallisation of margin borrower's credit risk. The Investment Committee of the Bank is responsible for managing equity portfolio in line with the policies and the guidelines as set out by the Board and the BIRMC. Allocation of limits for equities taken as collateral for loans and margin trading activities of customers and for the Bank's investment/trading portfolio forms part of the tools for managing the equity portfolio. Rigorous appraisal, proper market timing and close monitoring of the portfolio performance in relation to the market performance facilitates the management of the equity portfolio within the framework of Investment Strategy and the Risk Policy.

Liquidity Risk

Liquidity risk is the risk of not having sufficient funds to meet financial obligations in time and in full, at a reasonable cost. Liquidity risk arises from mismatched maturities of assets and liabilities. The Bank has a well set out framework for liquidity risk management and a contingency funding plan. The liquidity risk management process includes regular analysis and monitoring of the liquidity position by ALCO and maintenance of market accessibility. Regular cash flow forecasts, liquidity ratios and maturity gap analysis are used as analytical tools by the ALCO. Any negative mismatches up to the immediate three months revealed through cash flow gap statements are matched against cash availability either through incremental deposits or committed lines of credit. Whilst meeting the regulatory requirements relating to liquidity, for internal monitoring purposes, the Bank takes into consideration the liquidity of each eligible instrument relating to the market at a given point in time as well as undrawn commitments to borrowers when stress testing its liquidity position.

The maintenance of a strong credit rating and reputation in the market enables the Bank to access domestic wholesale funds. For short-term liquidity support, the Bank also has access to the money market at competitive rates. In line with the long-term project financing business, the Bank focuses on long-term funding through dedicated credit lines while its commercial banking business focuses on Current and Savings Accounts (CASA) and Term Deposits as the key source of funding for its lending. The structure and procedures for Asset and Liability Management at the Bank have been clearly set out in the Board approved ALCO Charter, which is reviewed on an annual basis.

The CBSL Direction No. 07 of 2011 specifies that liquidity can be measured through stock or flow approaches. Under the stock approach, liquidity is measured in terms of key ratios which portray the liquidity in the Balance Sheet. Under the flow approach banks should prepare a statement of maturities of assets and liabilities placing all cash inflows and outflows in the time bands according to their residual time to maturity in major currencies. The Bank has adopted both methods in combination to assess liquidity risk.

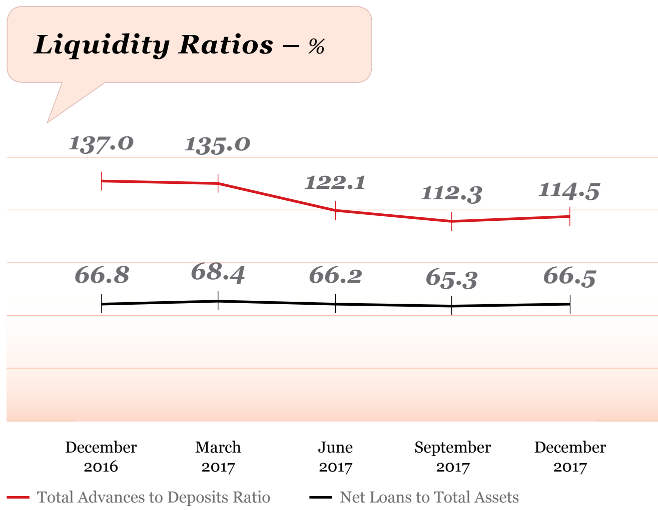
Liquidity Risk Management under Flow Approach

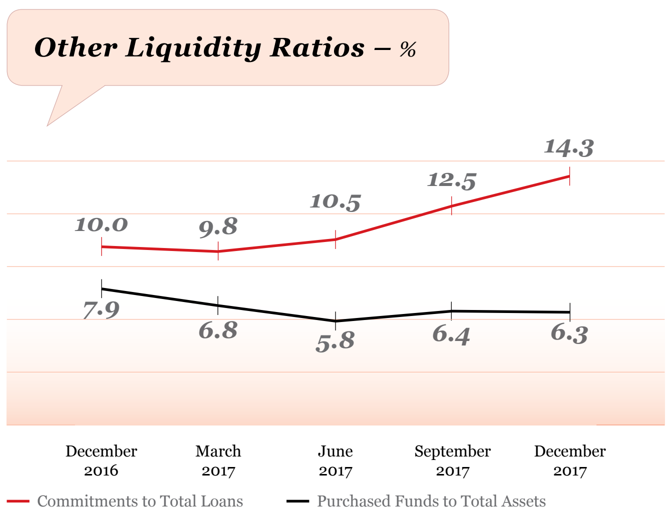
A Statement of Maturities of Assets and Liabilities (MAL) is prepared by the Bank placing all cash inflows and outflows in the time bands according to their residual time to maturity and non-maturity items as per CBSL recommended and the Bank specific behavioural assumptions.

The gap analysis of assets and liabilities provide the cash flow mismatches which assist in managing the liquidity obligations in a prudential manner.

Liquidity Ratios Under Stock Approach

The Bank regularly reviews the trends of the following ratios for liquidity risk management under the Stock approach in addition to the regulatory ratios. During the year, the Bank maintained liquidity indicators comfortably within regulatory minimums and the internal limits defined by the Risk Appetite statement.





The minimum liquidity standards (Liquidity Coverage Ratio) under Basel III were implemented from April 2015. Accordingly, banks are required to maintain an adequate level of unencumbered High Quality Liquid Assets (HQLAs) that can be easily and readily converted into cash to meet their liquidity needs for a 30-calendar day time horizon under a significantly severe liquidity stress scenario. The computations of LCR performed for the Bank indicated that the Bank was comfortably in compliance with the Basel III minimum requirement, shaving sufficient High Quality Liquid Assets well in excess of the minimum requirements specified by the Central Bank throughout the year. (The minimum requirement is 80% of HQLAs to be maintained over the immediate 30-day net cash outflow for the year 2017.)

The Central Bank of Sri Lanka (CBSL) has issued consultative guidelines for Net Stable Funding ratio (NSFR) in November 2017 to be implemented from April 2018. NSFR standards are designed to reduce funding risk over a longer time horizon by requiring banks to fund with sufficiently stable sources to mitigate the risk of future funding stress and requires banks to maintain a stable funding profile in relation to the composition of their assets and off-balance sheet exposures.

Key Liquidity Risk Measurement Tools and Reporting Frequencies

Liquidity risk measure/indicator	Minimum Frequency
Stock approach – Ratio analysis	
Net loans to total assets	Quarterly
Loans to customer deposits	Quarterly
Liquid assets to short-term liabilities	Quarterly
Large liabilities to earnings assets excluding temporary investments	Quarterly
Purchased funds to total assets	Quarterly
Commitments to total assets	Quarterly
Trends in the statutory liquid assets ratio	Monthly
Trends in Liquidity Coverage Ratio (LCR) and forecasts	Monthly
Flow approach	
Maturity gap report	Quarterly
Net funding requirement	Quarterly
Scenario analysis and stress testing	Quarterly
Contingency funding plan	Annual review

The Bank has in place a contingency plan which provides guidance on managing liquidity requirements in stressed conditions based on different scenarios of severity. The Contingency Funding Plan provides guidance in managing liquidity in bank specific or market specific scenarios. It outlines how assets and liabilities of the Bank are to be monitored, pricing strategies are to be devised and growth strategies to be reconsidered emphasising avoidance of a liquidity crisis based on the risk level. The management and reporting framework for ALCO identifies evaluating a set of early warning signals both internal and external in the form of a Liquidity Risk Matrix on a monthly basis in order to assess the applicable scenario ranging from low risk to extreme high liquidity risk and proposes a set of strategies to avoid and mitigate possible crises proactively. The action plan for each of the high risk contingency level scenarios is to be considered by a liquidity contingency management team which includes the CEO, Head of Treasury, CRO and a few other members of Senior Management. During the year, the Bank did not come across a high liquidity risk scenario and the Bank had sufficient standby liquidity facility agreements (Reciprocal agreement) to buffer against sudden liquidity stresses.

Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, systems, and external events. It covers a wide area ranging from losses arising from fraudulent activities, unauthorised trade or account activities, human errors, omissions, inefficiencies in reporting, technology failures or from external events such as natural disasters, terrorism, theft, or even political instability. The objective of the Bank is to manage, control and mitigate operational risk in a cost effective manner consistent with the Bank's risk appetite. The Bank has ensured an escalated level of rigour in operational risk management approaches for sensitive areas of its operations.

The Operational Risk Management Committee (ORMC) oversees and directs the management of operational risk of the Bank at an operational level with facilitation from the Operational Risk Management Unit (ORMU) of the IRMD. Active representation of the relevant departments and units of the Bank has been ensured in the process of operational risk management through the Operational Risk Coordination Officers.

Segregation of duties with demarcated authority limits, internal and external audit, strict monitoring facilitated by the technology platform and back-up facilities for information are the fundamental tools of operational risk management. Audit findings and management responses are forwarded to the Board's Audit subcommittee for their examination. Effective internal control systems, supervision by the Board, Senior Management and the line managers forms part of First Line of Defense for operational risk management at the Bank. The Bank demands a high level of technical skills, professionalism and ethical conduct from its staff and these serve as insulators for many operational risk factors.

The following are other key aspects of the operational risk management process at DFCC Bank PLC:

- Monitoring of Risk and Control Self-Assessment (RCSA) and Key Risk Indicators (KRIs) for the functions under defined threshold limits using a 'Traffic Light' system
- Maintaining internal operational risk incident reporting system and carrying out an independent analysis of the incidents by IRMD to recognise necessary improvements in the systems, processes and procedures
- Trend analysis on operational risk incidents and review at the ORMC and the BIRMC
- Review of downtime of the critical systems and assessment of the reasons. The necessary risk and business impact is evaluated. Rectification measures are introduced whenever the tolerance levels are compromised
- Review of HR attrition and exit interview comments in detail including a trend analysis with the involvement of the IRMD. The key findings of the analysis are evaluated at the ORMC in an operational risk perspective
- Reporting on grievances and investigation reports on Whistleblowing discussed at ORMC
- Establishment of the Bank's complaint management process under the Board approved Complaints Management Policy. IRMD analyses the complaints received to identify any systemic issues and reports to ORMC
- Conduct product and process reviews in order to identify the operational risks and recommend changes to the products and related processes
- Evaluate the operational risks associated with any new product developments
- Established an external loss database in order to take proactive action to mitigate operational risks that may arise from the external environment
- Assist in the Business Continuity Planning and Disaster Recovery (DR) processes and review the results of DR drills conducted in the Bank to provide recommendations for future improvements
- Conduct Fraud Risk Management Committee meetings periodically in order to identify potential fraud risks that might impact the Bank and to take timely remedial actions

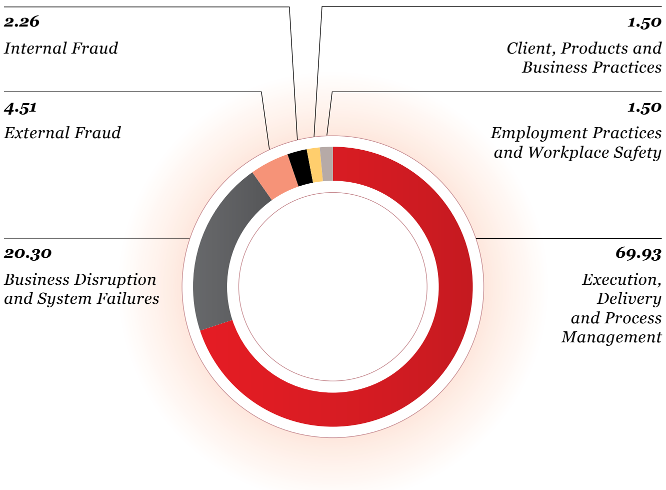
Operational Risk Reporting		
Risk Identification	Risk Assessment	Risk Monitoring and Controlling
– Risk and Control Self-Assessments (RCSA) – Operational Risk Incident Analysis (External and internal) – Risk Analysis of products/services – Analysis of customer complaints	– Evaluation of risks against the controls through RCSA – Key Risk Indicators (KRIs) – Incident Assessment and Escalation (Internal and external) – Stress testing	– Action plans based on incident analysis, RCSA and KRI – Insurance – Business Continuity Plan and periodic testing
Culture and Awareness		
Policies and Guidelines		

Operational Risk Losses

The Bank has improved its operational risk incident reporting system overtime by creating an increased level of awareness among the employees with regard to operational risks and the importance of incident reporting. A total of 133 incidents have been reported in 2017. The Bank has in place a well streamlined process of reporting in which the incidents could be reported by any employee of the Bank through an online portal. The Operational Risk Coordination officers (ORCO) are also expected to send a monthly report to the Operational Risk Management Unit regarding operational risk related incidents if any taken place at their respective branches or departments.

The operational risk incidents reported in 2017 based on the event type are categorised below:

Operational Risk Incidents – %



The majority of the incidents reported were as a result of a failure in the execution, delivery and process management, and they included near misses and no losses. However, the actual losses resulting from the operational risk events have been very marginal and there have been no significant losses incurred as a result of the existing stringent controls that are in place.

Risk and Control Self-Assessments (RCSA) and Key Risk Indicators (KRIs) Process of the Bank

Monitoring of Risk and Control Self-Assessments (RCSA) and Key Risk Indicators (KRIs) across all the departments and branches of the Bank, was further strengthened during the year as a measure to allow the early detection of operational risks before actual failure occurs.

RCSA requires self-evaluation of operational risk exposures of processes in the Bank by respective departments semi-annually. Each department will assess the risks based on impact and likelihood of occurrence. While controls are assessed based on control design and control performance. The risk exposure is derived through the level of risk compared to control effectiveness. The results are evaluated at ORMC for additional controls or mitigants in order to minimise risk exposure to the Bank.

Regular KRI monitoring, assists business line managers by providing them a quantitative, verifiable risk measurement which will be evaluated against the thresholds. A summary of KRIs are presented to ORMC based on a traffic light system.

Insurance as a Risk Mitigant

Insurance policies are obtained to transfer the risk of low frequency and high severity losses which may occur as a result of events such as fire, theft/frauds, natural disasters, errors and omissions. Insurance plays a key role as an operational risk mitigant in banking context due to the financial impact that any single event could trigger.

Insurance policies in force covering losses arising from undermentioned assets/processes include

- Cash and cash equivalents
- Pawned articles
- Premises and other fixed assets
- Public liability
- Employee infidelity
- Negligence
- Personal accidents and workmen's compensation

The Insurance Unit of the Bank reviews the adequacy and effectiveness of insurance covers on an annual basis and carries out comprehensive discussions with insurance companies on any revisions required at the renewal of the insurance covers.

Outsourcing of Business Functions

Outsourcing takes place when the Bank uses another party to perform non-core banking functions that would traditionally have been undertaken by the Bank itself. As a result, the Bank will be benefitted in focusing on its core banking activities while having the non-core functions being taken up by outside experts.

The Bank has outsourced some business functions under its Outsourcing Policy after evaluating whether the services are suitable for outsourcing based on assessment of the risks involved. Further, undertaking due diligence tests on the companies concerned such as credibility and ability of the owners, BCP arrangements, technical and skilled manpower capability and financial strength. Cash transportation, archival of documents, certain IT operations, security services, and selected recovery functions are some of the outsourcing activities of the Bank. The Bank is concerned and committed in ensuring that the outsourced parties continue to uphold and extend the high standard of customer care and service excellence.

A comprehensive report on outsourced activities is periodically submitted to CBSL for their review while adhering to Banking Direction on Outsourcing of Business Operations.

Key Operational Risk Measurement Tools and Reporting Frequencies

Operational Risk Measure/Indicator	Frequency
Operational risk incidents reported during the period (External and internal)	Quarterly
Risk and Control Self-Assessments and Key Risk Indicators	Semi-annually
Status and reports of any BCP/DR activities undertaken	As required
Customer complaints during the period	Quarterly
System and ATM downtime reports	Quarterly

Management of Information Systems Security (ISS) Risk Under IRMD

The objectives of ISS risk management are to be compliant with regulatory and contractual requirements, establish best practices and information security governance across the Bank, align information security risk management with the Bank's corporate risk management objectives and preserve Confidentiality, Integrity and Availability (CIA) requirements in the organisation's information assets. This is an ongoing process of discovering, correcting and preventing security weaknesses, where the Bank has adopted ISO 27001:2013 and PCI Data Security Standards for supporting the purpose.

The ISS Unit has taken up the following key responsibilities of the Information Security Management process at DFCC Bank PLC:

- Establish and manage the Information Security Management System (ISMS) based on ISO 27001:2013 and PCI-Data Security Standards.
- Development of information security policies, procedures and guidelines according to information security standards.
- Identification of security risks related to the Bank's information assets and projects and propose or implement controls to maintain residual risks at acceptable levels.
- Management of information security incidents and periodic information security risk assessments.
- Set and monitor information security KPIs and report the status of the indicators to the Information Technology Steering Committee (ITSC) and ORMC
- Perform trend analysis on information security incidents and reporting, which are regularly reviewed at the ORMC and the BIRMC

The established Information Security Management System provides a systematic approach to managing sensitive company information by covering all aspects including people, processes, technology and information systems.

Reputational Risk

Reputational risk is the risk of losing public trust or tarnishing of the Bank's image in the public eye. It could arise from environmental, social, regulatory, or operational risk factors. Events that could lead to reputational risk are closely monitored, utilising an early warning system that includes inputs from frontline staff, media reports, and internal and external market survey results. Though all policies and standards relating to the conduct of the Bank's business have been promulgated through internal communication and training, a specific policy was established to take action in case of an event which hinders the reputation. The Bank has zero tolerance for knowingly engaging in any business, activity, or association where foreseeable reputational damage has not been considered and mitigated. While there is a level of risk in every aspect of business activity, appropriate consideration of potential harm to the Bank's good name is a part of all business decisions. The complaint management process and the Whistleblowing Process of the Bank include a set of key tools to recognise and manage reputational risk.

Business Risk

Business risk is the risk of deterioration in earnings due to the loss of market share, changes in the cost structure and adverse changes in industry or macroeconomic conditions. The Bank's medium-term strategic plan and annual business plan form a strategic roadmap for sustainable growth. Continuous, competitor and customer analysis and monitoring of the macroeconomic environment enables the Bank to formulate its strategies for growth and business risk management. Processes such as Planning, ALM, IT and Product Development in collaboration with business functions facilitate the management of business risk through recognition, measurement, and implementation of tasks. Business risk relating to customers is assessed in the credit rating process and is priced accordingly.

Legal Risk

Legal risk arises from unenforceable transactions in a court of law or the failure to successfully defend legal action instituted against the Bank. Legal risk management commences from prior analysis, and a thorough understanding of, and adherence to related legislation by the staff. Necessary precautions are taken at the design stage of transactions to minimise legal risk exposure.

In the event of a legal risk factor, the Legal Unit of the Bank takes immediate action to address and mitigate these risks. External legal advice is obtained or counsel retained when required.

Compliance Risk

Compliance risk can be termed as the risk of legal or regulatory sanctions, financial losses, or damage to the reputation of the Bank as a result of its failure to comply with all applicable laws, regulations, Codes of Conduct and standards of good practice. The Bank ensures that effective compliance policies and procedures are followed and appropriate corrective actions are taken to rectify any breaches of laws, rules and standards as and when identified. A robust compliance culture has been established within the Bank with processes and work flows designed with the required checks and balances to facilitate compliance. The compliance function works closely with the business and operational units to ensure consistent management of compliance risk.

Compliance is a key area of focus during the process of new product development and review. The Head of Compliance submits quarterly reports on the compliance status to BIRMC and the Board, to enable oversight to be exercised with the added safeguard of being subject to internal audit. A culture of compliance permeates all levels of the Bank with regular training and knowledge sharing provided by internal as well as external experts in the area.

Anti-Money Laundering (AML)/Combating Terrorist Financing (CTF)

In response to international best practices and global standards, Sri Lanka has enacted laws relating to AML and CTF. Further, the Financial Intelligence Unit, under the purview of the Central Bank, has issued rules for the Know Your Customer (KYC) and Customer Due Diligence (CDD) processes, to identify and report suspicious transactions. The Bank has taken necessary measures to implement these regulatory and legislative requirements for AML and CTF. The steps taken in this regard include customer identification and verification, maintenance of records, ascertaining sources of funds, monitoring and maintenance of AML/CTF programmes. The customers of the Bank are subject to appropriate KYC/CDD measures.

Business Continuity Management

The Business Continuity Plan (BCP) of the Bank ensures timely recovery of critical operations that are required to meet stakeholder needs based on identified disruptions categorised into various severity levels. BCP has been designed to minimise risk to human and other resources and to enable the resumption of critical operations within reasonable time frames specified according to Recovery Time Objectives (RTOs) with minimum disruption to customer services and payment and settlement systems. The Disaster Recovery site, which is located in a suburb of Colombo is used for periodic testing drills. These DR drills are subject to independent validation by the Internal Audit Department. A report on the effectiveness of the drill is submitted to the BIRMC/Board and also to the Central Bank with their observations. Learnings and improvements to disaster recovery activities are discussed and implemented through the ORMC and BIRMC. Training is carried out to ensure that employees are fully aware of their role within the BCP.

Stress Testing of Key Risks

DFCC Bank PLC has been conducting stress testing on a regular basis. The Bank has in place, a comprehensive Stress Testing Policy and Framework, which is in line with the regulatory guidelines as well as international best practices. The Policy describes the purpose of stress testing and governance structure and the methodology for formulating stress tests, whilst the framework specifies in detail the Stress Testing programme including the stress tests, frequencies, assumptions, tolerance limits and remedial action.

Stress testing and scenario analysis have played a major role in the bank’s Risk Mitigating Policy. Stress testing has provided a dynamic platform to assess, “What If” scenarios and to provide the Bank with an assessment on areas to improve. The Bank covers a wide range of stress tests that check the resilience of the Bank's capital, liquidity, profitability etc.

The outcome of stress testing process is monitored carefully and remedial actions taken and used by the Bank as a tool to supplement other risk management approaches.

The details of stress tests carried out by the Bank as at 31 December 2017 are given below:

Risk Area and Methodologies Adopted	Results Evaluated
Credit and Concentration Risk → Impact of increase in the Non-Performing Assets (NPAs) → Impact to the Bank due to fall in value of collaterals of NPA → Sector Concentration, Concentration of Credit Ratings, Concentration of Products, Concentration of Borrowers such as the top 10 clients	→ Capital ratio was stressed to see if the ratio falls below the regulatory level → Additional capital was computed for all extreme concentration risks and was reported to Senior Management
Market Risk → Stress VAR of currency exposure → Stress VAR for equity portfolio → Change of interest rates and its effect on Bank's profitability and capital	→ VAR on currency exposure and equity portfolio were within the Bank's acceptable risk matrices → Change of interest rates did not affect the capital of the Bank in a serious manner
Operational Risk → Stress Bank's capital against increase of possible operational losses	→ No significant effect on capital and is well within the Bank's risk absorption capability
Liquidity Risk → Stress on liquidity due to settlement risks, decline in collections and bulk deposit redemption → Stress on Liquid Asset Ratio due to run of in liquid liabilities → Erosion of deposits due to sudden reputational risk and associated liquidity risks	→ Liquid Asset Ratio was maintained above 20% at low level of shock while slightly falls below at medium level of shock. At high level of shock the ratio can fall below 20%, which is extreme and highly unlikely
Multi Factor Stress Testing → Combined stress of all risks	→ Except for the worst case scenario the regulatory capital was not breached. The worst case scenario is an extreme scenario where all types of risks will emerge under extreme conditions at the same time

The findings of the Bank's stress testing activities are an input into several processes including capital computation under Internal Capital Adequacy Assessment Process (ICAAP), strategic planning and risk management among others. As an integral part of ICAAP under Pillar II, stress testing is used to evaluate the sensitivity of the current and forward risk profile relative to the stress levels which are defined as low, moderate and high in the Stress Testing Policy. The resultant impact on the capital through these stress tests is carefully analysed and the BIRMC conducts regular reviews of the stress testing outcomes including the major assumptions that underpin them.

As it provides a broader view of all risks borne by the Bank in relation to its risk tolerance and strategy in a hypothetical stress situation, stress testing has become an effective communication tool to Senior Management, Risk Owners and Risk Managers as well as Supervisors and Regulators. The results of the stress testing are reported to the BIRMC and the Board on a quarterly basis for appropriate and proactive decision making.

DFCC Bank's Risk Capital Position and Financial Flexibility

The Bank adopts a proactive approach to ensure satisfactory risk capital level throughout its operations. In line with its historical practice and the capital targets, the Bank aims to maintain its risk capital position higher than the regulatory minimum requirements for Tier I and total capital under Basel guidelines.

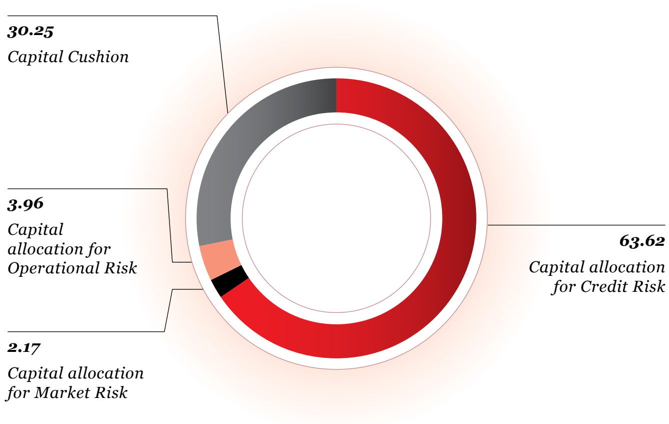
As at 31 December 2017, DFCC Bank PLC maintains a healthy risk capital position of 12.68% Tier I capital ratio and 16.13% total capital ratio based on the Basel III regulatory guidelines. This demonstrates a cushion of about 5.43% and 4.88%, respectively, for Tier I and total capital over the minimum regulatory requirements.

Capital adequacy measures the adequacy of the Bank's aggregate capital in relation to the risk it assumes. The capital adequacy of the Bank has been computed under the following approaches of the Basel regulations which are currently effective in the local banking industry:

- Standardised approach for credit risk
- Standardised approach for market risk
- Basic Indicator approach for operational risk

The graph below shows the Bank's capital allocation and available capital buffer as at 31 December 2017, based on the quantified risk as per the applicable regulatory guidelines. Out of the regulatory risk capital (total capital) available as at 31 December, capital allocation for credit risk is 63.62% of the total capital while the available capital buffer is 30.25%.

***Capital Distribution** – %*



Capital Adequacy Management

BASEL III is the new global regulatory standard on managing capital and liquidity of banks which is currently in effect. With the introduction of BASEL III, the capital requirements of banks have increased with an aim to raise the quality, quantity, consistency and transparency of capital base and improve the loss absorbing capacity.

Additionally, the Pillar II (Supervisory Review Process – SRP) under the Basel regulations requires banks to implement an internal process, called the Internal Capital Adequacy Assessment Process (ICAAP), for assessing capital adequacy in relation to the risk profiles as well as a strategy for maintaining capital levels. The Bank has in place an ICAAP, which has strengthened the risk management practices and capital planning process. It focuses on formulating a mechanism to assess the Bank's capital requirements covering all relevant risks and stress conditions in a futuristic perspective in line with the level of assumed risk exposures through its business operations. The ICAAP formulates the Bank's capital targets, capital management objectives and capital augmentation plans.

The ICAAP of DFCC Bank PLC demonstrates that the Bank has implemented methods and procedures to capture all material risks and adequate capital is available to cover such risks. This document integrates Pillar I and Pillar II processes of the Bank wherein Pillar I deals with regulatory capital, primarily covering credit. Market and operational risks whilst Pillar II deals with economic capital involving all other types of risks.

As per the direction issued by CBSL, under supervisory review of Basel III, CBSL encourages banks to enhance their risk management framework and manage emerging risks in a more proactive manner. This is to ensure that the Bank maintains adequate capital buffer in case of a crisis while more importance has been placed on Pillar II and ICAAP. The Bank uses a mix of quantitative and qualitative assessment methods to measure Pillar II risks. A quantitative assessment approach is used for concentration risk, liquidity risk and interest rate risk whilst qualitative approaches are used to assess the reputational risk and strategic risk.

The Senior Management team is closely involved in formulating risk strategy and governance, thereby considering the Bank's capital planning objectives under the strategic planning process. Capital forecasting for the next three years covering envisaged business projections is considered in the budgeting process. This forward-looking capital planning helps the Bank to be ready with additional capital requirements in the future. It integrates strategic plans and risk management plans with the capital plan in a meaningful manner with inputs from Senior Management, Management Committees, Board Committees and the Board.

The Banking Act Direction No. 01 of 2016 introduced capital requirements under Basel III for Licensed Commercial Banks, commencing from 1 July, 2017 with specified timelines to increase minimum capital ratios to be fully implemented by 1 January, 2019. The capital forecast performed under the ICAAP process has indicated the ability of the Bank to maintain a comfortable level of capital cushion in the next few years, while proposing suitable capital augmentation plans. Basel II Capital guidelines have been revoked by CBSL with the implementation of Basel III guidelines from mid 2017.

Capital Adequacy Ratio and Risk-Weighted Assets of DFCC Bank PLC on a Solo and Group Basis Under Basel III

Quantified as per the CBSL Guidelines	31 December 2017		31 December 2016	
	Bank	Group	Bank	Group
Credit Risk-Weighted Assets (LKR million)	**237,482**	**237,671**	194,737	195,094
Market Risk-Weighted Assets (LKR million)	**8,110**	**8,110**	3,169	3,169
Operational Risk-Weighted Assets (LKR million)	**14,783**	**15,508**	15,512	16,252
Total Risk-Weighted Assets (LKR million)	**260,375**	**261,289**	213,418	214,515
Total Tier I Capital Adequacy Ratio – Basel III*	**12.68%**	**13.09%**	13.80%	15.43%
Total Capital Adequacy Ratio – Basel III*	**16.13%**	**16.53%**	18.11%	19.72%

** Basel III capital ratios became effective from 1 July 2017. Information presented for 31 December 2016 are based on parallel computation.*

Financial Flexibility in the DFCC Group's Capital Structure

The Bank has access to contributions from shareholders as well as to built-up capital over a period of time by adopting prudent dividend policies, maintaining an increased level of retained profits and issuing Tier II eligible capital instruments as and when necessary. The Bank is reasonably comfortable with the current and future availability of capital buffer to withstand an ambitious growth or stressed market conditions.

Apart from the strong capital position reported On-Balance Sheet, the Group maintains financial flexibility through the stored value in its equity investment portfolio. The unrealised capital gain of the listed equity portfolio is included in the Fair Value Reserve and currently a part has been taken into consideration in the capital adequacy computation under Basel III based on regulatory specifications.

Assessment of Integrated Risk

In the process of assessment of integrated risk, the Bank reviews key regulatory developments in order to anticipate changes and their potential impact on performance. The nature and impact of changes in economic policies, laws and regulations, are monitored and considered in the way the Bank conducts business and manages capital and liquidity.

The Bank has complied with all the currently applicable risk-related internal requirements in addition to the regulatory requirements as shown in the table below:

Risk Category	Impact	Key Risk Indicators	Regulatory/Internal Limit	Position as at 31 Dec. 2017
Integrated Risk Management	An adequate level of capital is required to absorb unexpected losses without affecting the Bank's stability.	Common Equity Tier I Ratio (Common Equity Tier I as a percentage of total risk-weighted assets)	Regulatory	Complied
		Total Tier I Capital Ratio (Total Tier I capital as a percentage of total risk-weighted assets)	Regulatory	Complied
		Total Capital Ratio (Total capital as a percentage of total risk-weighted assets)	Regulatory	Complied

Risk Category	Impact	Key Risk Indicators	Regulatory/Internal Limit	Position as at 31 Dec. 2017
Concentration/ Credit Risk Management	When the credit portfolio is concentrated to a few borrowers or a few groups of borrowers with large exposures, there is a high risk of a substantial loss due to failure of one such borrower.	Single Borrower Limit – Individual (Amount of accommodation granted to any single company, public corporation, firm, association of persons, or an individual/capital base)	Regulatory	Complied
		Single Borrower Limit – Group	Regulatory	Complied
		Aggregate large accommodation (Sum of the total outstanding amount of accommodation granted to customers whose accommodation exceeds 15% of the capital base/outstanding amount of accommodation granted by the Bank to total customers excluding the Government of Sri Lanka)	Regulatory	Complied
		Aggregate limits for related parties (Accommodation to related parties as per the CBSL Direction/Regulatory Capital)	Internal	Complied
		Exposure to agriculture sector (As per CBSL Direction)	Regulatory	Complied
		Exposure to each industry sector (On-Balance Sheet exposure to each industry as a percentage of total Lending Portfolio)	Internal	Complied
		Exposure to selected regions (On-Balance Sheet exposure to the regions as a percentage of the Total Lending Portfolio)	Internal	Complied
		Leases Portfolio (On-Balance Sheet exposure to the leasing product as a percentage of Total Lending Portfolio Plus Securities Portfolio)	Internal	Complied
		Exposure to Government of Sri Lanka	Internal	Complied
		Non-Performing Ratio	Internal	Complied
		Industry HHI	Internal	Complied
		Maximum expected loss limits for each product line	Internal	Complied
		Loan and OD – Exposure in BB and below grades	Internal	Complied
		Loan and OD – Exposure in B and below grades	Internal	Complied
		Leasing – Exposure in BB and below grades	Internal	Complied
		Leasing – Exposure in B and below grades	Internal	Complied
		Target rating-wise PDs and provisions	Internal	Complied
		Margin trading (Aggregate exposure of margin loans extended/total loans and advances)	Internal	Complied
Liquidity Risk Management	If adequate liquidity is not maintained, the Bank will be unable to fund the Bank's commitments and planned assets growth without incurring costs or losses.	Liquid Asset Ratio for DBU (Average monthly liquid assets/ total monthly liabilities)	Regulatory	Complied
		Liquid Asset Ratio for FCBU	Regulatory	Complied
		Liquidity Coverage Ratio (All currencies and Rupee only)	Regulatory	Complied
		Single Depositor Limit (Highest Single Depositor/Total fixed deposits)	Internal	Complied
		Net interbank borrowing exposure	Internal	Complied
Market Risk Management		Forex Net Open Long Position	Regulatory	Complied
		Forex Net Open Short Position	Regulatory	Complied
		Limit for counterparty Off-Balance Sheet Market Risk	Internal	Complied
		Limit for settlement risk arising from market risk	Internal	Complied
		Maximum holding period for trading portfolio	Internal	Complied
		Treasury trading securities portfolio	Internal	Complied

Risk Category	Impact	Key Risk Indicators	Regulatory/Internal Limit	Position as at 31 Dec. 2017
Investment Risk		Equity exposure – Individual (Equity investment in a private OR public company/Capital funds of the Bank)	Regulatory	Complied
		Equity exposure – Individual (Equity investment in a private OR public company/Paid-up capital of the Company)	Regulatory	Complied
		Aggregate equity exposure in public companies (Aggregate amount of equity investments in public companies/Capital funds of the Bank)	Regulatory	Complied
		Equity exposure (Equity exposure as a percentage of Total Lending Portfolio Plus Securities Portfolio)	Internal	Complied
		Equity exposure in each sector	Internal	Complied
		Single equity exposure	Internal	Complied
Operational Efficiency		Operational Efficiency Ratio	Internal	Complied
Operational Risk	Adequately placed policies, processes and systems will ensure and mitigate excessive risks which may result in direct financial impact, reputational damages and/or regulatory actions.	Reputational risk of the Bank and Group (Zero risk appetite)	Internal	Complied
		Significant regulatory breaches (Zero risk appetite)	Internal	Complied
		Inability to recover from business disruptions over and above the Recovery Time Objectives (RTO) as defined in the BCP of the Bank (Zero risk appetite)	Internal	Complied
		Mis-selling of financial products and services (Zero risk appetite)	Internal	Complied
		Failure to undertake risk-based customer due diligence (Zero risk appetite)	Internal	Complied
		Internal fraud (Zero tolerance for losses due to acts of a type intended to defraud, misappropriate property or circumvent regulations, the law or bank policy, excluding diversity/discrimination events, which involves at least one internal party)	Internal	Complied
		External fraud (Very low appetite for losses due to act of a type intended to defraud, misappropriate property or circumvent laws, by a third party)	Internal	Complied
		Employee practices and workplace safety (Zero appetite for losses arising from acts inconsistent with employment, health or safety laws or agreements from payment of personal injury claims, or from diversity/discrimination events)	Internal	Complied
		Client products and business practices (Zero risk appetite for losses arising from an unintentional or negligent failure to meet a professional obligation to specific clients (including fiduciary and suitability requirements) or from the nature or design of a product)	Internal	Complied
		Damage to physical assets (Very low appetite for losses arising from loss or damage to physical assets from natural disaster, or other events)	Internal	Complied
		Business disruption and systems failures (Very low appetite for business disruptions)	Internal	Complied
		Execution, delivery, and process management (Very low appetite for losses from failed transaction processing or process management)	Internal	Complied

Corporate Governance

Chairman's Statement

Corporate governance practices of the Bank are in accordance with the Board approved Corporate Governance Charter of the Bank.

The Bank's corporate governance framework is well structured and is supported by a strong focus on integrity, transparency and clear and timely communication. We endeavour to ensure that our policies and procedures comply with the applicable Corporate Governance Direction of the Central Bank of Sri Lanka and other relevant laws. Furthermore, the Bank's corporate governance structure supports our business and meets the needs of our stakeholders.

The Board sets the example for employees of the Bank by implementing the highest standards of business ethics and corporate governance. I confirm to the best of my knowledge that there were no material violations of any of the provisions of the Directions of the Central Bank of Sri Lanka, other applicable laws and regulations, Codes of Conduct and other related policies and procedures of the Bank.

C R Jansz
Chairman

19 February 2018

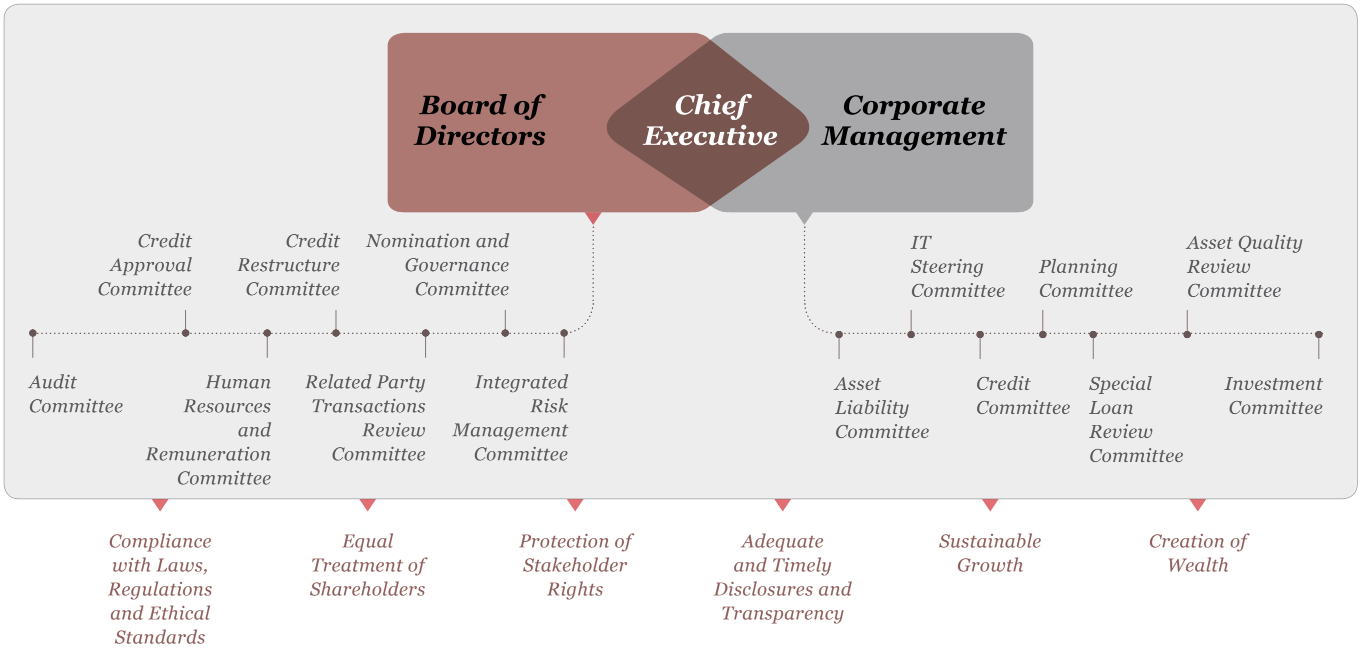
Governance Framework of the Bank

Good corporate governance is a mechanism that harmonises the interests of a wide range of stakeholders of an institution, while contributing to sustainable growth by attracting outside sources of capital. The Bank practices high standards of corporate governance based on the OECD principles of good governance.

OECD principles of good governance are based on the following six guidelines:

- Promoting transparency, being consistent with laws and clearly articulating division of responsibilities
- Protecting and facilitating the exercise of shareholder rights and ensuring equitable treatment of all shareholders
- Exercising due diligence and responsibility in capital market operations
- Recognising the rights of stakeholders and encouraging co-operation between stakeholders in creating wealth and sustainability
- Timely and accurate disclosure on all material matters regarding the Bank including financial situation, performance, ownership and governance
- Ensuring the strategic guidance of the Bank, effective monitoring of management of the Board, and the Board's accountability to the Bank and its shareholders

DFCC Bank's Goals of Good Corporate Governance



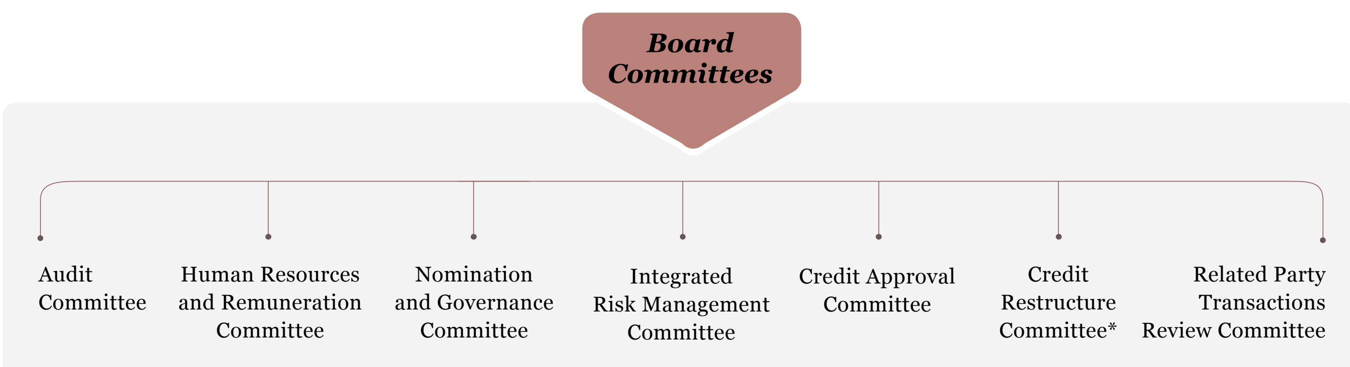
Conduct and Ethical Framework

The Code of Conduct for Directors adopted by the Bank which the Directors are expected to abide by, encompasses the following:

- Compliance with laws, rules and regulations
- Avoidance of conflict of interests
- Maintenance of confidentiality of information
- Fair dealing with stakeholders
- Protection of Banks assets

Employee behaviour is governed by a separate Code of Conduct including other policies and procedures such as the Disciplinary Code, Statement Prohibiting Insider Trading, Whistleblowing Policy, Anti-Money Laundering Policy, Compliance Policy, Disclosure Policy etc.

Permanent Board Committees as at 31 December 2017



** The Credit Restructure Committee approves papers by circulation.*

Name of Director	Attendance of Directors at Meetings						
	Main Board	Audit Committee	Human Resources and Remuneration Committee	Nomination and Governance Committee	Integrated Risk Management Committee	Credit Approval Committee	Related Party Transactions Review Committee
Total No. of Meetings	14	16	8	7	4	13	12
H A Ariyaratne	3/3				1/1		
K D N R Asoka	10/10	10/12			3/3		
K P Cooray	13/14		3/4	6/7		10/13	8/12
T Dharmarajah	14/14	15/16			1/1	11/11	12/12
A R Fernando	8/8				1/2		1/6
Ms L K A H Fernando	1/2	2/3			1/1		
P M B Fernando	14/14	14/16		7/7	3/3	2/2	
C R Jansz	14/14		8/8	7/7		13/13	12/12
Ms V J Senaratne	14/14		4/4		3/3		
L H A L Silva	14/14				2/2		6/6
Ms S R Thambiayah	13/14		8/8				
L N de S Wijeyeratne	11/11	11/12			3/3		

Shareholder Rights

The basic rights of shareholders include – (a) the ability to transfer shares freely, (b) to have access to financial and other relevant information about the entity on a regular and timely basis, (c) the ability to effectively participate in shareholder meetings, (d) appoint Directors and Auditors, and (e) equitable treatment relating to the type of shares owned.

The shares of the Bank are freely transferable through the Colombo Stock Exchange but subject to limitations stated in the Articles of Association of the Bank and the Banking Act.

The Board approved Corporate Communications Policy ensures that information relating to the financial performance and the progress of the Bank is made available to shareholders through timely disclosures made to the Colombo Stock Exchange (CSE). The Annual Report contains a comprehensive review of performance as well as other information of relevance to the other stakeholders apart from reporting on the financial condition of the Bank and the Group. All important information is given publicity through the press and electronic media and posted on the Bank's website.

The Bank has procedures to promptly disseminate price sensitive information and trading in shares by the Directors to the CSE as required by the Listing Rules. In instances where this is not possible, the Chief Financial Officer advises closed periods for trading in Bank's shares by employees and Directors. The Board has formally adopted a Statement of Policy Prohibiting Insider Trading. As a general rule, the period after the end of each quarter up until two market days after the financial information is released, is treated as closed periods. Procedures are in place to detect any violations.

During the year under review, the Bank has shared a reasonable portion of its profit with shareholders in the form of a dividend while retaining the balance to support its growth and development.

All shareholders of the Bank are treated equally on the basis of one vote per ordinary share. The Bank has not issued any non-voting ordinary shares or preference shares.

Annual General Meeting

The Annual General Meeting of the Bank is normally held within a period of one year from the date of the previous meeting after giving adequate notice to shareholders as required by the Articles of Association. The Annual Report and Notice of Meeting are sent to all shareholders in order to enable effective shareholder participation at the meeting. Shareholders have the opportunity to obtain the Annual Report as an electronic or printed document. Extraordinary General Meetings are held to obtain shareholder approval on matters that require such approval.

Annual Corporate Governance Report for the Year ended 31 December 2017 published in terms of Section 3 (1) (xvi) of the Banking Act Direction No. 11 of 2007

Rule	Governance Principle	Compliance	Remarks
3.1 Responsibilities of the Board			
3.1 (i)	Safety and soundness of the Bank The Board has strengthened the safety and soundness of the Bank through the implementation of the following:		
	(a) Strategic objectives and corporate values	Compliant	The Bank sets its strategic objectives and goals through the Annual Business Plan which is approved by the Board. These goals and the corporate values approved by the Board are communicated to the business units and other staff. The corporate values are posted on the internal web and all employees are guided by these values.
	(b) Overall business strategy	Compliant	The Bank's strategic plan for the medium term was approved by the Board in January 2017. The Board engages in the strategic planning and control of the Bank by overseeing the formulation of business objectives and targets, assessing risks by engaging qualified and experienced personnel, delegating them with the authority for conducting operational activities and monitoring the performance through a formal reporting process. A separate item has been included in the agenda at every Board meeting under the heading "Strategic Discussion" to take up any matter of strategic importance to the Bank. Directors are encouraged to identify and communicate any matter they consider to be of strategic importance.
	(c) Principal risks	Compliant	The identification of principal risks, approving of overall Risk Policy and risk appetite is carried out through the Board Integrated Risk Management Committee and reviewed annually.
	(d) Communication with stakeholders	Compliant	The Board approved Corporate Communications Policy ensures that information is made available to shareholders and other stakeholders through timely disclosures made to the Colombo Stock Exchange (CSE), by publicity through the press and electronic media and posts on the Bank's website. The Bank has an internally developed Code of Conduct for its employees which is posted on the internal web and is accessible by all employees.
	(e) Bank's internal control and management information systems	Compliant	The Audit Committee assists the Board in reviewing and evaluating the integrity, adequacy and effectiveness of the internal control system including management information systems and controls over financial reporting of the Bank. The Internal Audit carries out periodic reviews to ensure that the internal control systems are functioning as appropriate. The Report by the Board of Directors on internal control over financial reporting is given on page 140. The Independent Assurance Report by the External Auditor on the Directors Statement on Internal Control is given on page143.
	(f) Key Management Personnel (KMP)	Compliant	The Board has identified and designated its Key Management Personnel.

Rule	Governance Principle	Compliance	Remarks
	(g) Authority and responsibility	Compliant	Areas of authority and key responsibilities of Directors have been set out in the Corporate Governance Charter which has been adopted by the Board. The Board has also identified matters specifically reserved for the Board. The duties and responsibilities of other KMPs are formally documented in their job descriptions. Delegation of authority levels for KMPs have also been clearly specified in Board approved circulars.
	(h) Oversight of the affairs of the Bank by KMPs	Compliant	Oversight is exercised through Board committees, reporting to the Board as appropriate. Policies and decisions of the Board requiring appropriate follow up are communicated by the Board Secretary to the relevant KMPs. Minutes of relevant management committee meetings headed by the Chief Executive Officer (CEO) are submitted to the Board for information. KMPs are called upon to clarify matters and make presentations on matters within their purview at the monthly Board meetings.
	(i) Board's own governance practices	Compliant	An annual self-assessment is carried out on a structured format where the Directors submit their individual responses direct to the Company Secretary. The responses are collated by the Company Secretary and submitted to the Board. The effectiveness of the Board's own governance practices are reviewed by the Board and areas for improvement are discussed for necessary action. During the year, in addition to the assessments carried out by the individual members, the Nomination and Governance Committee, based on a separate checklist, carried out an evaluation of the Board and the results were shared with the other members of the Board and an opportunity was provided to them to comment on the findings of the Committee.
	(j) Succession plan for KMPs	Compliant	The Bank has in place a succession plan for senior management which is reviewed annually by the Nomination and Governance Committee and approved by the Board. During the year, in order to improve the process for succession planning for KMPs, a committee was formed comprising a member of the Audit Committee, CEO and Head of HR.
	(k) Regular meetings with KMPs to monitor progress	Compliant	Meetings are attended by relevant executives when required. Additional information sought by Directors on papers submitted to the Board is clarified by the respective officers. The Board has free access to Senior Management. The business initiative Board committees established to drive key business areas relating to CASA, lending, SME business, investments and media and branding, continued to function during the year and the members of these committees met KMPs on a regular basis to review the status of implementation of identified strategies. During the year, the Board held quarterly review meetings in order to monitor progress against the business plan. These meetings provided an opportunity for the Board members to interact with the Senior Management to clarify reasons for variations against the budget and to suggest corrective action.

Rule	Governance Principle	Compliance	Remarks
	(l) Regulatory environment	Compliant	The Board Secretary provides all regulatory information required to the Board members. The CEO briefs the Board on specific issues. Senior management maintains continuous dialogue with the Regulator to ensure an effective relationship.
	(m) Due diligence in hiring and oversight of External Auditor	Compliant	The primary responsibility for making recommendations on the appointment of the External Auditor rests with the Audit Committee. A formal policy approved by the Board on engagement of External Auditor to perform non-audit services is in place.
3.1 (ii)	Appointment and segregation of the roles of the Chairman and CEO	Compliant	The Board elects the Chairman and appoints the CEO. While the Chairman provides leadership to the direction, oversight and control process exercised by the Board, the CEO is responsible for management of the Bank.
3.1 (iii)	Board meetings	Compliant	The Board held 14 Board meetings during the year. The Directors actively participated in the Board's decision-making process as evident from the Board minutes. Seeking approval of the Board by disseminating of circulars was done only in exceptional circumstances due to urgency.
3.1 (iv)	The Board to ensure that arrangements are in place for Directors to include items and proposals in the agenda of Board meetings	Compliant	Whenever the Directors suggest topics for consideration at the Board meetings, they are included in the agenda under 'open discussion' which is an integral part of every Board meeting and other supporting data, reports, documents etc. relevant for the subject matter are circulated among the Directors for information.
3.1 (v)	Notice of Board meetings – At least seven days notice of regular meetings and reasonable notice of other meetings to be given	Compliant	Dates for the regular monthly Board meetings are agreed by the Directors at the start of each year and any changes to dates of scheduled meetings are decided well in advance. The Board Circulars and other documents pertaining to meetings are made available well in advance to enable the Directors to participate in deliberations.
3.1 (vi)	Attendance at Board meetings	Compliant	All Directors attended more than two-thirds of Board meetings and no Director was absent for three or more consecutive meetings. Attendance details are given on page 113.
3.1 (vii)	Duties and qualifications of the Company Secretary	Compliant	The Company Secretary possesses the qualifications specified in Section 43 of the Banking Act. The Company Secretary while performing the secretariat services to the Board and shareholders' meetings, is responsible to the Board in ensuring that Board procedures and applicable rules and regulations are followed. All new Directors are provided with the necessary documentation on Directors' responsibilities and specific banking-related directions/ policies that are required to perform their function effectively.
3.1 (viii)	The Directors' access to the Company Secretary	Compliant	All Directors have access to the advice and services of the Company Secretary directly.
3.1 (ix)	The Company Secretary's duty to maintain minutes of Board meetings and ensure the Directors' access to them	Compliant	The Company Secretary compiles the minutes of the Board meetings which are subject to approval of the Board and signed by the Chairman and the Secretary. Copies of minutes are provided and Directors have access to the original minute at all reasonable times.

Rule	Governance Principle	Compliance	Remarks
3.1 (x)	The form and contents of the minutes of Board meetings	Compliant	The Board minutes are drawn with reference to Board Circulars with sufficient details to indicate the decisions made by the Board of Directors. The information used in making such decisions, the reasons and rationale of making them and each Director's contribution, if considered material, is included in the minutes.
3.1 (xi)	Independent professional advice on request for Directors to perform their duties	Compliant	The Board has put in place a procedure where the Directors can obtain independent professional advice, at the Bank's expense, to perform their duties.
3.1 (xii)	The Directors' avoidance of conflict of interest	Compliant	The Companies Act No. 07 of 2007 require Directors who are directly or indirectly interested in contracts or a proposed contract with the Bank to declare the nature of such interest. The Directors have declared their interests in contracts involving the Bank and have not participated in the decision-making.
3.1 (xiii)	Schedule of matters reserved for the decisions of the Board	Compliant	Schedule of matters reserved for the Board have been decided on.
3.1 (xiv)	Reporting insolvency to the Director of Bank Supervision	Compliant	Solvency is a matter constantly monitored by the Treasury Department, Integrated Risk Management Committee and the Board of Directors. During the year under review, the Bank remained solvent and no event has or is likely to occur that would make the Bank not able to meet its obligations.
3.1 (xv)	Adequacy of capital	Compliant	The Bank is capitalised well above the minimum levels required by the Monetary Board in terms of the capital adequacy and minimum required capital.
3.1 (xvi)	Corporate Governance Report	Compliant	The annual Corporate Governance Report forms an integral part of the Directors Report of the Bank's Annual Report.
3.1 (xvii)	Self-assessment of the Board of Directors	Compliant	The Board has a structured scheme of self-assessment which is carried out annually. The performances of the respective committees are also evaluated by the other members who are not members of the respective committees in order to ensure that they function effectively. The findings are discussed at the Board meetings and action is taken on areas identified for improvement. The performance assessment criteria of the CEO is given in 3.5 (xi).
3.2 Composition of the Board			
3.2 (i)	Number of Directors	Compliant	The Board of Directors comprised eight Directors at the end of the year under review.
3.2 (ii)	Period of service of a Director	Compliant	No Director has held the position of a Director of the Bank for more than nine years.
3.2 (iii)	Number of Executive Directors	Compliant	The CEO is the only Executive Director on the Board.
3.2 (iv)	Number of Independent Directors	Compliant	There were five Independent Directors at the end of the year under review.

Rule	Governance Principle	Compliance	Remarks
3.2 (v)	Alternate Directors to represent Independent Directors	Compliant	Persons who are appointed as Alternate Directors to existing Independent Directors of the Board are subject to the same criteria applicable to such Directors. During the year, Independent Directors did not appoint any Alternates.
3.2 (vi)	The skills, experience and track records of Non-Executive Directors	Compliant	Non-Executive Directors who held office had professional backgrounds, strong track records and high level managerial experience in banking, business, industry, law, finance or auditing.
3.2 (vii)	Number of Non-Executive Directors required to form a quorum of Board meetings	Compliant	The Bank has been compliant with this rule at all times as monitored by the Company Secretary.
3.2 (viii)	Disclosure of details of Directors	Compliant	The names and the composition of the Directors by category are disclosed in the Annual Report of the Board of Directors.
3.2 (ix)	Appointments of new Directors	Compliant	Appointments of new Directors are formally evaluated by the Nomination and Governance Committee and recommended to the Board of Directors for approval.
3.2 (x)	Appointment of a Director to fill a casual vacancy	Compliant	The Articles of Association of the Bank provide that the Directors appointed by the Board of Directors hold office until the following AGM at which they have to be elected by the shareholders.
3.2 (xi)	Resignation or removal of a Director	Compliant	The details of retirement/resignation of Directors from office during the year under review are given in the Directors' Report. No Director was removed during the year under review. There were no matters that needed to be brought to the attention of the shareholders as a consequence of the resignation of H A Ariyaratne and K D N R Asoka since they resigned due to their personal wish.
3.2 (xii)	Appointment of a Director or an employee to another bank	Compliant	No Director or employee of the Bank is a Director of another bank.
3.3 Fitness and Propriety of Directors			
3.3 (i)	Maximum age of Directors	Compliant	All Directors who reached the age of 70 have relinquished office.
3.3 (ii)	Holding of Director's position in more than 20 companies in all	Compliant	All Directors comply with this requirement.
3.4 Management Functions Delegated by the Board			
3.4 (i)	Delegation arrangements	Compliant	The Board of Directors has delegated authority to the management subject to specific criteria, limitations, safeguards and monitoring mechanisms.
3.4 (ii)	Extent of delegation	Compliant	The delegation of authority made by the Board is designed to facilitate efficient management of the affairs of the Bank and to aid the oversight role exercised by the Board. It is not of an extent to hinder the ability of the Board to discharge its functions. The Board retains the authority to expand, curtail, limit or revoke such delegated authority.

Rule	Governance Principle	Compliance	Remarks
3.4 (iii)	Review of delegation process	Compliant	The delegation process is subject to periodic review by the Board in order to ensure that necessary amendments are approved to meet the requirements of the Bank. Material decisions made under delegated authority are reported to the Board for information.
3.5 The Chairman and Chief Executive Officer			
3.5 (i)	Separation of the roles of the Chairman and CEO	Compliant	The Chairman and the CEO are two separate individuals.
3.5 (ii)	The Chairman to be a Non-Executive Director	Compliant	The Chairman is a Non-Executive Director. The Board appointed an Independent Director as the Senior Director as disclosed in the Annual Report. The Board has approved Terms of Reference for the Senior Director.
3.5 (iii)	Disclosure of relationship between the Chairman, CEO and other Directors	Compliant	No relationships exist between the Chairman, CEO and the other Directors according to the declarations made by them except being Directors of subsidiaries, and the Chairman and one other Director being on the Board of two companies outside the Group.
3.5 (iv)	Role of the Chairman	Compliant	The Chairman provides leadership to the Board and ensures that the Board discharges its responsibilities effectively. The Chairman encourages members to actively participate and to raise their independent judgment on all key and appropriate issues in a timely manner.
3.5 (v)	Agenda of Board meetings	Compliant	The Agenda of each Board meeting is drawn by the Company Secretary under the direction of CEO and Chairman and any matters relevant to the policies and operations of the Bank proposed by other Directors are included in the Agenda upon approval by the Chairman.
3.5 (vi)	Providing information to the Directors	Compliant	The Chairman ensures that all Directors are properly briefed on issues which arise at the Board meetings and ensures that they receive adequate information in a timely manner.
3.5 (vii)	The Board to act in the best interest of the Bank	Compliant	The Chairman encourages exercise of independent judgment by the Directors on matters under consideration by the Board in order that the best interests of the Bank can be assured.
3.5 (viii)	Effective contribution of Non-Executive Directors	Compliant	The Chairman facilitates contributions by the Non-Executive Directors in making decisions.
3.5 (ix)	The Chairman not to engage in executive functions	Compliant	The Chairman is Non-Executive and does not supervise any management personnel of the Bank directly.
3.5 (x)	Communication with shareholders	Compliant	The Chairman has assigned the CEO to maintain a dialogue with institutional investors and to bring any matters of concern to the notice of the Board. The Communications Policy approved by the Board includes a provision for communication with shareholders.
3.5 (xi)	CEO to be in charge of the management of operations and business	Compliant	The CEO is the Head of the management team and is in charge of day-to-day management of the Bank's operations and business. At the beginning of each year, the Board discusses the business plan with the CEO and Senior Management, and agrees on the medium and short-term financial and non-financial targets to be achieved and action plans to be implemented by the Bank. Progress is monitored on an ongoing basis and the assessment of the performance of the Bank is carried out by the Board at the end of each year based on the initiatives laid down in the business plan.

Rule	Governance Principle	Compliance	Remarks
3.6 Board Appointed Committees			
3.6 (i)	Four Board appointed committees	Compliant	The Board has appointed the four committees required by the Direction. The reports on their duties, performance and roles are published in the Annual Report.
3.6 (ii)	Board Audit Committee		Please refer page 131.
	(a) Chairman of the Committee	Compliant	During the year under review, the Audit Committee was chaired by an Independent Non-Executive Director who is a qualified Chartered Accountant.
	(b) Composition of the members	Compliant	All members of the Committee are Non-Executive Directors.
	(c) External Auditor	Compliant	The Audit Committee assists the Board in implementing a transparent process in the engagement and remuneration of the External Auditor and assists in the general oversight of financial reporting, internal controls and compliance with laws, regulations and Codes of Conduct. The Committee ensures that the engagement of the audit partner does not exceed five years.
	(d) Independence and effectiveness of the audit process	Compliant	The Committee reviewed the statement issued by the External Auditor pursuant to Section 163 (3) of the Companies Act No. 07 of 2007. The Committee discussed with the External Auditors, the nature and scope of the audit, and the effectiveness of the audit process in respect of the Financial Year 2017.
	(e) Non-audit services	Compliant	A formal policy approved by the Board on Engagement of the External Auditor to perform non-audit services is in place.
	(f) Nature and Scope of external audit	Compliant	The Committee met with the External Auditor to discuss and finalise the scope of the audit to ensure that it is in compliance with guidelines issued by the Central Bank of Sri Lanka.
	(g) Review of financial information of Bank	Compliant	The Committee reviewed all quarterly non-audited interim Financial Statements and the financial statement for the year ended 31 December 2017.
	(h) Meetings with External Auditor	Compliant	The Committee met with the External Auditor on seven occasions and at two meetings without the presence of the management.
	(i) Review of Management Letter	Compliant	The Committee considered the Management Letter issued by the External Auditor for the period ended 31 December 2016 and the management responses thereto.
	(j) Internal Audit function	Compliant	The Committee reviews the adequacy of the Internal Audit function to ensure that it is in conformity with the Audit Committee Charter. The annual audit plan is approved by the Committee. The plan covers the scope and resource requirement. The annual performance appraisal of the Head of Internal Audit and the senior staff members are reviewed by the Committee. The Committee, with the approval of the Board continued to supplement the Internal Audit function by engaging two firms of Chartered Accountants to carry out the periodic audits of some business units. The Internal Audit function is independent of the activities it audits and the findings are reported directly to the Audit Committee.

Rule	Governance Principle	Compliance	Remarks
	(k) Internal Audit findings	Compliant	The Committee reviewed the Internal Audit Reports and considered the findings, recommendations and corrective action.
	(l) Attendance of non-audit committee members	Compliant	Vice President – Internal Audit attends all Committee meetings. CEO, Deputy CEO, CFO, other Heads of units and the External Auditors attend meetings on invitation. During the year, the Committee met with the External Auditor on two occasions without the presence of the Executive Directors.
	(m) Terms of Reference	Compliant	The Committee is guided by the Audit Committee Charter.
	(n) Meetings	Compliant	During the financial year ended 31 December 2017, 16 meetings were held. Attendance of Committee members is given in the table on page 113.
	(o) Audit Committee activities	Compliant	Please refer Committee Report on page 131.
	(p) Secretary	Compliant	Vice President – Internal Audit serves as the Secretary of the Committee.
	(q) Process of raising issues in confidence	Compliant	The Board has adopted a Whistleblowing Policy to encourage employees to communicate legitimate concerns on any illegal or unethical practices. Arrangements are in place to ensure that all employees are duly informed of the effective use of this process.
3.6 (iii)	Board Human Resources and Remuneration Committee		Please refer page 134.
	(a) Remuneration Policy	Compliant	A formal Remuneration Policy approved by the Board is in place.
	(b) Goals and targets for KMPs	Compliant	The business plan which is approved by the Board encompasses the annual goals and targets of the CEO and other Key Management Personnel.
	(c) Review of performance of KMPs	Compliant	The Committee annually reviews the performance against the set targets of the CEO and other KMPs and the remuneration levels of the CEO and other KMPs, while ensuring appropriate compensation levels are maintained in order to retain and motivate staff.
	(d) CEO's presence	Compliant	The CEO attends meetings by invitation and participates in deliberations except when matters relating to him are discussed.
3.6 (iv)	Board Nomination and Governance Committee		Please refer page 135.
	(a) Appointment of new Directors and KMPs	Compliant	During the year, the Committee considered and recommended to the Board, the appointment of two new Directors and candidates to fill Key Management Positions. The Committee also reviewed and documented the procedure to select/appoint Directors and other KMPs.
	(b) Re-election of Directors	Compliant	During the year, the Committee considered and recommended to the Board, the re-election of the Directors retiring under Articles 44 and 46 (ii) while ensuring that they are fit and proper persons to hold such office.
	(c) Criteria relating to appointment of KMPs	Compliant	The Committee evaluates the qualifications, experience and key attributes required for eligibility for appointment of KMPs. During the year, the Committee reviewed and incorporated necessary changes to the job descriptions of the respective KMPs.
	(d) Fit and proper test	Compliant	The fitness and propriety of KMPs are monitored by the Committee.

Rule	Governance Principle	Compliance	Remarks
	(e) Succession planning	Compliant	The Committee evaluates the need for additional/new expertise to the Board and succession for retiring KMPs.
	(f) Composition	Compliant	The Committee consists of three Non-Executive Directors and is chaired by an Independent Director.
3.6 (v)	Board Integrated Risk Management Committee (BIRMC)		Please refer page 136.
	(a) Composition	Compliant	Please refer page 136.
	(b) Assessment of risk	Compliant	The Committee has put in place a Board approved risk framework. The risk exposures of the Bank are assessed on a monthly basis through Key Risk Indicators. The risk assessment of subsidiaries, joint venture and the associate are reviewed quarterly.
	(c) Review of Adequacy of Management Committees	Compliant	The Committee assesses the effectiveness of all Management Committees.
	(d) Controlling risks within prudent limits	Compliant	The Committee assesses possible risks, reviews and takes appropriate action to mitigate such risks.
	(e) Frequency of meetings	Compliant	The Committee met on a quarterly basis.
	(f) Corrective action on any management failure to identify risks	Compliant	Action is taken by the Committee with regard to any officer responsible for failure to identify specific risks, and appropriate corrective action is taken to remedy such situations.
	(g) Submission of Risk Assessment Reports to the Board	Compliant	By submitting BIRMC minutes, the Board is informed of proceedings. The required approvals are obtained through specific submissions to the Board.
	(h) Compliance function	Compliant	The compliance function is headed by a dedicated officer identified as a KMP in terms of the Corporate Governance Direction. The Compliance Officer reports to the BIRMC. The Committee overseas the function and reviews the quarterly reports on compliance.
3.7 Related Party Transactions			
3.7 (i) to (iii)	Avoidance of conflicts of interest and favourable treatment in transactions with related parties	Compliant	The Bank has adhered to the law as specified in the Banking Act and the Directions issued thereunder with regard to transactions with related parties. The Board ensures that no related party benefits from any favourable treatment except as indicated in 3.7 (vi). A Related Party Transactions Review Committee has been established by the Board. The Board has also adopted a Policy on Related Party Transactions. The Bank has put in place a mechanism to obtain, on a quarterly basis, a confirmation from all Key Management Personnel on a structured format to assist in the process of collating related party transactions.
3.7 (iv)	Accommodation granted to Directors or their close relations	Compliant	The Bank complies with the law as specified in the Banking Act and the Directions issued thereunder in granting accommodation to the Directors and/or their close relations.
3.7 (v)	Accommodation granted to Directors prior to appointment	Compliant	The provisions of the Banking Act will be followed if such situations arise and public will be informed if not compliant by the specified date as he/she will cease to hold office. This situation did not arise.

Rule	Governance Principle	Compliance	Remarks
3.7 (vi)	Avoidance of favourable treatment in granting accommodation to employees, close relations of employees and/or entities in which any employee or close relation of such employee hold substantial interest	Compliant	The accommodation granted to employees, close relations of employees and/or entities in which any employee or close relation of such employee holds substantial interest are subject to normal commercial terms applicable to such transactions and secured by security approved by the Monetary Board except in the case of accommodation under approved schemes, uniformly applicable to all or specific categories of employees.
3.7 (vii)	Not to remit part of accommodation or interest without prior approval of Monetary Board	Compliant	No such situation has arisen.

Disclosure on Corporate Governance made in Terms of Section 3 (8) of the Banking Act Direction No. 11 of 2007 of the Central Bank of Sri Lanka

(i) The Board shall ensure that:		
	The annual audited Financial Statements and quarterly Financial Statements are prepared and published in accordance with the formats prescribed by the supervisory and regulatory authorities and applicable accounting standards, and such statements are published in the newspapers in an abridged form in Sinhala, Tamil and English.	Complied with.
(ii) The Board shall ensure that the following minimum disclosures are made in the Annual Report:		
(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.	Complied with. Please refer the Statement of Directors' Responsibility on page 149.
(b)	A Report by the Board on the Bank's internal control mechanism that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting and that the preparation of Financial Statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.	Complied with. Please refer to the Directors' Statement of Internal Control on page 140.
(c)	The External Auditor's Certification on the effectiveness of the internal control mechanism in respect of any statements prepared or published after 31 December 2008.	Complied with. Please refer Assurance Report of the External Auditor on page 143.
(d)	Details of Directors, including names, fitness and propriety, transactions with the Bank and the total fees/remuneration paid by the Bank.	Complied with. Please refer to pages 16, 17 and 126 and Note 55.7 to the Financial Statements.

(e)	Total net accommodation as defined in 3 (7) (iii) granted to each category of related parties shall also be disclosed as a percentage of the Bank's regulatory capital	Complied with.

Category of related party	31 December 2017 LKR 000	%
Key Management Personnel and Close family members	44,136	0.11
Total net accommodation	44,136	0.11
Regulatory capital – solo basis	41,993,352	

The total net accommodation was 0.11% of the Bank's regulatory capital on solo basis. Maximum limit determined by Directors is 25% of the Bank's regulatory capital on solo basis.

(f)	The aggregate values of remuneration paid by the Bank to its Key Management Personnel and the aggregate values of the transactions of the Bank with its Key Management Personnel, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the Bank.	Complied with. The aggregate value of compensation and transactions with the Bank by Key Management Personnel as defined by LKAS 24 for financial reporting purposes are given in Note 55.7 to the Financial Statements. Further, in addition to the above, compensation, total deposits and investments made and accommodation obtained as at 31 December 2017 by the other Key Management Personnel (officers performing executive functions referred to in Banking Act Determination No. 3 of 2010) amounted to LKR 92.2 million, LKR 162.5 million and LKR 21.3 million respectively.
(g)	All findings of the "Factual Findings Report" of the External Auditor to be incorporated in this Report.	Complied with.
(h)	A Report setting out details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any material non-compliance.	Complied with. See Annual Report of the Board of Directors.
(i)	A statement of the regulatory and supervisory concerns on lapses in the Bank's risk management, or non-compliance with these Directions that have been pointed out by the Director of Bank Supervision, if so directed by the Monetary Board to be disclosed to the public, together with the measures taken by the Bank to address such concerns.	The Monetary Board has not required any disclosure to be made.

Independent Assurance

The External Auditors have performed procedures set out in Sri Lanka Related Services Practice Statement 4750 (SLRSPS 4750) issued by The Institute of Chartered Accountants of Sri Lanka, to meet the compliance requirement of the Corporate Governance Direction. Their findings presented in their Report addressed to the Board are consistent with the matters disclosed above and did not identify any inconsistencies to those reported above by the Board.

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

Constitution

DFCC Bank was incorporated in 1955 under the DFCC Bank Act No. 35 of 1955, as a limited liability public company and the ordinary shares of the Bank were listed on the Colombo Stock Exchange.

Consequent to the enactment of the DFCC Bank (Repeal and Consequential Provisions) Act No. 39 of 2014, the DFCC Bank Act No. 35 of 1955, was repealed and with effect from 6 January 2015, the Bank was incorporated under the Companies Act No. 07 of 2007 as a Public Limited Company listed on the Colombo Stock Exchange with the name "DFCC Bank PLC".

The shareholders at the Extraordinary General Meeting held on 28 August 2015, approved the amalgamation of DFCC Vardhana Bank PLC (DVB) with DFCC Bank PLC (Bank). The Registrar General of Companies on, 1 October 2015 issued the Certificate of Amalgamation in terms of Section 244 (1) (a) of the Companies Act No. 07 of 2007 that DVB has been amalgamated with DFCC Bank PLC in accordance with the provisions of Part VIII of the Companies Act, with DFCC Bank PLC surviving as the amalgamated entity.

DFCC Bank PLC also obtained a commercial banking license from the Monetary Board of the Central Bank of Sri Lanka in terms of the Banking Act No. 30 of 1988, as amended, and accordingly upon the amalgamation now operates as a Licensed Commercial Bank with effect from 1 October 2015.

Going Concern

The Directors are satisfied that the Bank has adequate resources to continue its operations in the future and as such, the Financial Statements are prepared on the basis of a going concern. The Auditors have declared the Bank solvent even after the payment of dividend.

Financial Statements

The Financial Statements of the Bank and the Group are given on pages 152 to 244 of the Annual Report.

The Financial Statements of the Bank and the Group have been prepared in accordance with Sri Lanka Accounting Standards prefixed SLFRS and LKAS, the Banking Act No. 30 of 1988 and amendments thereto, the Companies Act No. 07 of 2007 and other applicable statutory and regulatory requirements.

Review of Business for the Year

The Chairman's Statement, Chief Executive's Review and the Management Discussion and Analysis give details of the operations of the Bank and the Group, and the key strategies that were adopted during the year under review.

Profit and Appropriations

Year ended 31 December 2017	LKR 000
Profit for the period	4,414,964
Appropriations	
Transfer to Reserve Fund (statutory requirement)	220,000
First and final dividend approved for financial year ended 31 December 2017	1,325,488
Unappropriated profit for the period	2,869,476

Accounting Policies

The accounting policies adopted in the preparation of the Financial Statements of the Bank and the Group are stated on pages 161 to 244 of the Annual Report.

There were no changes to the accounting policies of the Group in the year under review.

Auditors' Report

The Auditors' Report on the Financial Statements, which is unqualified, is given on page 151.

Reappointment of Auditors

The present Auditors, Messrs KPMG have expressed their willingness to continue as Auditors of the Bank for the next financial year ending 31 December 2018. The Audit Committee has reviewed the effectiveness and the relationship with the Bank including the fees paid to the Auditors and has concluded that they are suitable to continue in office. The Directors are satisfied that based on the written representation made by the Auditors, they have no relationship or interest with the Bank or with any of its subsidiaries which would impair the Auditors' independence. A Resolution pertaining to their reappointment and authorising the Directors to determine their remuneration will be proposed at the Annual General Meeting for adoption.

The Board of Directors

The Board of Directors of the Bank presently consist of nine Directors with wide knowledge and experience in the fields of banking and finance, trade, law, commerce, manufacturing or services. Profiles of the Directors are given on pages 16 to 17. During the year, L H A L Silva, Deputy CEO/Director assumed duties as the Chief Executive Officer/Ex-Officio Director with effect from 16 August 2017.

The Directors of the Bank categorised in accordance with criteria specified in the Direction No. 11 of 2007 issued by the Central Bank of Sri Lanka are as follows:

Non-Executive Directors

C R Jansz – Chairman
N K G K Nemmawatta*
Ms V J Senaratne

Independent Non-Executive Directors

K P Cooray
T Dharmarajah
Ms L K A H Fernando
P M B Fernando – Senior Director
Ms S R Thambiayah

Executive Director

L H A L Silva – Chief Executive Officer

** Appointment in terms of Article 36 (ii) of the Articles of Association*

N K G K Nemmawatta represents a specific stakeholder and as such does not qualify to be designated as an Independent Director.

C R Jansz and Ms V J Senaratne also do not meet the criteria set out in the Direction to be designated as Independent Directors by virtue of the fact that Mr Jansz and Ms Senaratne are common Directors of two companies outside the Group.

Senior Director

P M B Fernando has been designated as the Senior Director in terms of Central Bank of Sri Lanka Direction on Corporate Governance.

Resignation and Retirement of Directors

A R Fernando retired from the Board with effect from 15 August 2017, on completion of his contract of employment. L N de S Wijeyeratne retired from the Board with effect from 28 October 2017 having served a period of nine years as a Director of the Bank. H A Ariyaratne and K D N R Asoka resigned from the Board with effect from 28 March 2017 and 10 October 2017 respectively.

The Directors' record their appreciation for the contributions made by them during their tenure as Directors.

Appointment and Re-election of Directors

Ms L K A H Fernando was appointed a Director with effect from 1 November 2017. N K G K Nemmawatta was appointed on 1 February 2018 to succeed K D N R Asoka.

Ms Fernando will retire in terms of Article 46 (ii) of the Articles of Association and is offering herself for re-election at the Annual General Meeting. The Nomination and Governance Committee has recommended her re-election and the Board having concluded that she is a fit and proper person to be a Director in terms of the provision of the Banking Act unanimously endorsed the recommendation of the Nomination and Governance Committee.

Retirement by Rotation and Re-election of Directors

The Directors retiring by rotation in terms of Article 44 of the Articles of Association are Ms V J Senaratne and P M B Fernando, who offer themselves for re-election under the said Article with the unanimous support of the Directors.

Directors' Remuneration

The Directors' remuneration in respect of the Bank and the Group for the financial year ended 31 December 2017 is given below:

	Year ended 31 December 2017 LKR 000	Year ended 31 December 2016 LKR 000
Bank	**80,877**	68,748
Group	**103,818**	90,223

Directors' Meetings

The Bank held 14 Board meetings during the year. The attendance of Directors is shown in the table on page 113 of the Annual Report.

Directors' Interests in Shares

	No. of Shares as at 31 December 2017	No. of Shares as at 31 December 2016
H A Ariyaratne[1]	–	102,710
K D N R Asoka[1]	–	Nil
K P Cooray	**Nil**	Nil
T Dharmarajah	**500**	500
A R Fernando[1]	–	4,470
Ms L K A H Fernando[2]	**Nil**	–
P M B Fernando	**1,000**	1,000
C R Jansz	**1,000**	1,000
Ms V J Senaratne	**1,296**	1,296
L H A L Silva	**3,476**	3,476
Ms S R Thambiayah	**Nil**	Nil
L N de S Wijeyeratne[1]	–	Nil

[1] *Not a Director as at 31 December 2017*
[2] *Not a Director as at 31 December 2016*

Directors' Interests in Debentures

	31 December 2017 LKR 000	31 December 2016 LKR 000
L H A L Silva	**2,000**	2,000

No Director directly or indirectly holds options of the Bank.

Directors' Interests Register

An interest register is maintained by the Bank as required by the Companies Act No. 07 of 2007. Directors have made the general disclosure as provided for in Section 192 of the Companies Act No. 07 of 2007. The Directors have declared all material interests in contracts involving the Bank and have not participated in the decision-making related to such transactions. All related entries were made in the interest register during the year under review.

Directors' Interests in Transactions with the Bank

The Directors' interests in transactions with entities/ persons (other than subsidiaries, the joint venture and associate) listed under each Director for the year ended 31 December 2017 is as follows:

	LKR '000
K P Cooray Hotel Developers Lanka PLC Aggregate amount of accommodation	4,608,000
The Associated Newspapers of Ceylon Limited Aggregate amount of payments made for services	456
T Dharmarajah DHS Medical Group (Pvt) Limited Aggregate amount of accommodation	490
A R Fernando LVL Energy Fund Limited Aggregate amount of accommodation	875,000
Credit Information Bureau of Sri Lanka Aggregate amount of payments made for services	6,921
Ms L K A H Fernando United Motors Lanka PLC Aggregate amount of payments made for supplies	30
C R Jansz Distilleries Company of Sri Lanka PLC Melstacorp PLC Aggregate amount of accommodation	4,000,000
Lanka Bell Limited Periceyl Limited Aggregate amount of payments made for services and supplies	5,571
Ms V J Senaratne Distilleries Company of Sri Lanka PLC Melstacorp PLC Aggregate amount of accommodation	4,000,000
L H A L Silva Aggregate amount of accommodation	2,000
Acuity Securities Limited LVL Energy Fund Limited Aggregate amount of accommodation	1,800,000
LVL Energy Fund Limited Aggregate amount of fee received for services rendered	8,941
Lanka Financial Services Bureau Limited Sri Lanka Banks Association (Guarantee) Limited Aggregate amount of payments made for services	4,358
L N de S Wijeyeratne Kelani Valley Plantations PLC L B Finance PLC Aggregate amount of accommodation	850,000

A R Fernando, K P Cooray and L H A L Silva are or have been Chairman/Director of one or more of the subsidiary, joint venture or associate companies. Details of transactions with subsidiary, joint venture and associate companies are disclosed in Notes 55.3 to 55.5 to the Financial Statements.

Corporate Donations

During the year, the Bank made donations amounting to LKR 10,600.

Board Committees

The following are the members of the permanent committees of the Board. Changes to the composition during the year are set out in the respective Committee Reports in the Annual Report:

Audit Committee

P M B Fernando – Chairman
T Dharmarajah
Ms L K A H Fernando

Credit Approval Committee

C R Jansz – Chairman
K P Cooray
P M B Fernando

Credit Restructure Committee

C R Jansz – Chairman
T Dharmarajah
Ms S R Thambiayah

Human Resources and Remuneration Committee

C R Jansz – Chairman
K P Cooray
Ms S R Thambiayah

Nomination and Governance Committee

P M B Fernando – Chairman
K P Cooray
C R Jansz

Integrated Risk Management Committee

T Dharmarajah – Chairman
Ms L K A H Fernando
Ms V J Senaratne
L H A L Silva

Chief Risk Officer of the Bank is also a member of the Committee.

Related Party Transactions Review Committee

T Dharmarajah – Chairman
K P Cooray
C R Jansz
L H A L Silva

In addition, from time to time the Board appoints committees to deal with specific matters. The Board also invites external advisors and Key Management Personnel to serve on some of the committees as and when necessary.

Further details relating to the committees are given in the section on Corporate Governance and the Committee Reports.

Dividend

The Directors have approved the payment of a first and final dividend of LKR 5.00 per share, (final dividend paid in the previous period, LKR 4.50 per share). The total dividend for the year will amount to approximately LKR 1,325 million (LKR 1,193 million in the previous period), which amounts to 32% of the Bank's distributable profit.

The Directors unanimously declare that, DFCC Bank PLC will satisfy the solvency test stipulated in Section 57 of the Companies Act No. 07 of 2007 immediately after the dividend payment is made and a certificate of solvency from its Auditor is obtained.

Property, Plant and Equipment and Leasehold Property

The total expenditure of acquisition on property, plant and equipment during the year amounted to LKR 880.9 million of which intangible assets amounted to LKR 275.6 million. Details of these are given in the Notes 38 and 39 to the Financial Statements.

Reserves

Total reserves and retained profit amounted to LKR 43,161 million.

Market Value of Freehold Properties

The information on market value of freehold properties are given in Note 38.1.2 to the Financial Statements.

Stated Capital and Subordinated Debentures

The stated capital as at 31 December 2017 was LKR 4,716 million. The number of shares in issue as at 31 December 2017 was 265,097,688. Further information is given on page 216.

Share Information

Information relating to earnings, net assets and market value per share are given on pages 54 and 144 of the Annual Report and also contains information pertaining to the share trading during the period.

Shareholders

As at 31 December 2017, there were 8,728 registered shareholders and the distribution is indicated on page 145.

The 20 largest shareholders as at 31 December 2017 are listed on page 146.

Employment and Remuneration Policies

The policy of the Bank is to develop and maintain a dedicated and highly motivated group of employees who are committed to creating sustainable value through effective risk management and high quality service while supporting public and private sector in its development efforts within the ambit of the Articles of Association of the Bank. DFCC Bank PLC continuously invests in training and development of its staff to meet these objectives. The Bank is an equal opportunity employer. Remuneration of employees consists of fixed and variable payments. Annual increments and pay awards are based on the performance of the Bank and the individual. It is the Bank's policy to fix remuneration at a level which will attract, motivate and retain high quality employees.

Statutory Payments

The Directors, to the best of their knowledge and belief are satisfied that all statutory payments due to the Government and in relation to the employees have been made on time.

Related Party Transactions

The Related Party Transactions Review Committee is responsible for ensuring compliance with the code specified in Section 9 of the CSE Listing Rules. The Committee reviewed the related party transactions carried out during the year and noted that the transactions were in compliance with the said code.

Compliance with Laws, Regulations and Prudential Requirements

DFCC Bank PLC has not engaged in any activities contravening the laws and regulations and has complied with prudential requirements. The Directors obtain quarterly, a confirmation report from the management with regard to compliance with laws, regulations and prudential requirements.

Events Occurring after the Reporting Period

Subsequent to the date of the statement of financial position, no circumstances have arisen which would require adjustments to the accounts. Significant events occurring after the reporting period which in the opinion of Directors require disclosure are described in Note 58 to the Financial Statements.

Corporate Governance

The Directors place great emphasis on following internationally accepted good corporate governance practices, and principles, and systems and procedures are in place in order to satisfy good governance requirements.

The Directors have obtained External Auditors' assurance on effectiveness of the internal control mechanism and compliance with the Direction No. 11 of 2007 of the Central Bank of Sri Lanka on Corporate Governance.

Details of governance practices and the required disclosures are given on pages 111 to 124.

Rule 3 (8) of the Direction No. 11 of 2007 on Corporate Governance for Licensed Commercial Banks in Sri Lanka prescribe disclosures in the Annual Report. These disclosures have been made in this Annual Report as shown in the following table:

The table below provides cross references to facilitate easy reference.

Reference to Rule	Requirement	Reference to Annual Report
3 (8) (i)	Financial Statements on prescribed format	Financial Statements on pages 152 to 244
3 (8) (ii) (a)	Affirmative assurance of compliance with accounting standards and requirements	Directors' Responsibility Statement on page 149
3 (8) (ii) (b)	Affirmative assurance of the integrity of financial reporting system	Directors' Statement of Internal Control on page 140
3 (8) (ii) (c)	Assurance report issued by the External Auditor	Independent Assurance Report on page 143
3 (8) (ii) (d)	Information on Directors	Pages 16 and 17
3 (8) (ii) (d)	Remuneration of Directors	Annual Report of the Directors on page 126
3 (8) (ii) (e)	Net accommodation granted to each category of related party	Corporate Governance Report. Table on page 124
3 (8) (ii) (f)	Compensation and other transactions with Key Management Personnel	Corporate Governance Report on page 124
3 (8) (ii) (h)	Compliance with prudential requirements and regulations	This report.

Acknowledgment of the Content of the Report

As required by Section 161 (1) (k) of the Companies Act No. 07 of 2007, the Board of Directors does hereby acknowledge the contents of this Report.

For and on behalf of the Board of Directors,

C R Jansz
Chairman

L H A L Silva
Director and Chief Executive Officer

Ms A Withana
Company Secretary

19 February 2018

Report of the Audit Committee

The Board Audit Committee comprises of three Independent Non-Executive Directors and one Non-Executive Director. The Committee is chaired by Mr P M B Fernando who is a Fellow of The Institute of Chartered Accountants of Sri Lanka and possesses considerable experience in the field of Finance and Auditing.

The members of the Board appointed Audit Committee are as follows:

P M B Fernando – Chairman

T Dharmarajah

L K A H Fernando

Brief profiles of the members are given on pages 16 to 17.

The following changes took place during the year in the Board Audit Committee. L N de S Wijeyeratne retired and K D N R Asoka resigned from the Board in October 2017 and Ms L K A H Fernando was appointed to the Audit Committee with effect from 1 November 2017.

Meetings

The Head of Group Internal Audit, functioned as the Secretary to the Committee for the year ended 31 December 2017. During the year, 15 Audit Committee meetings were held and proceedings of the Audit Committee meetings were reported regularly to the Board.

Attendance by the Committee members at the meetings is given in the table on page 113 of this Annual Report.

The Chief Executive Officer, Chief Financial Officer and Chief Operating Officer attend meetings by invitation. Senior Management also attend the meetings on invitation in order to brief the Audit Committee on specific matters. The Committee held two meetings with the External Auditor; KPMG independently, without the presence of executive management, to discuss the progress and conclusion of the Audit.

Mandate and Role

The Terms of Reference of the Committee, which is subject to review periodically by the Board of Directors, clearly defines the mandate and role of the Committee. The Committee is responsible to the Board of Directors and reports on its activities regularly. The Committee assists the Board of Directors in fulfilling its general oversight of financial reporting, internal controls, internal and external audits.

The Committee has discharged the responsibilities assigned by Rule No. 3(6) (ii) of the Corporate Governance Direction No.11 of 2007, issued by the Central Bank of Sri Lanka. Where appropriate, more details are provided under separate headings in this report.

Financial Reporting

The Committee reviews effectiveness of the financial reporting system in place, to ensure reliability of information provided to the stakeholders. The Committee reviews that to the best of its knowledge and belief, the Financial Statements issued for external purposes by DFCC Bank PLC (Bank), complied with generally accepted principles of accounting as enunciated in Sri Lanka Accounting Standards, and complies with the statutory provisions of Companies Act No. 07 of 2007 and Banking Act No. 30 of 1988 and subsequent amendments thereto.

The Committee assists the Board of Directors to discharge their responsibility for the preparation of true and fair Financial Statements in accordance with the books of accounts and Sri Lanka Accounting Standards. The Committee reviews the adequacy and effectiveness of the internal control system and procedures to provide reasonable assurance that all transactions are accurately and completely recorded in the books of accounts. In accordance with the mandate, the Committee reviewed and discussed with the management and Internal/External Auditors on the critical accounting policies, practices, related changes thereto, alternative accounting treatments, major judgement areas, material audit adjustments, compliance with accounting standards, going concern assumptions, financial reporting controls and compliance with applicable laws and regulations that could impact the Bank's Financial Statements, its annual report and its quarterly Financial Statements prepared for publication.

The Committee reviewed all quarterly non-audited interim Financial Statements and Financial Statements for the year ended 31 December 2017, together with supporting information that included significant assumptions and judgments made in the preparation of Financial Statements. The Committee also took into consideration the Internal Audit reports, management letter issued by the External Auditor and the responsibility statements in relation to the Financial Statements issued by the Chief Financial Officer and Chief Executive Officer in making an overall assessment on the integrity of the financial reporting system.

The Committee also discussed the operations, future prospects and sustainability indicators of the Bank with management regularly and is satisfied that all relevant matters have been taken into account in the preparation of the Financial Statements and that the 2017 Financial Statements are reliable and presents a true and fair view of the state of affairs of the Bank.

Internal Controls

The Audit Committee assessed the effectiveness of internal control over financial reporting as at 31 December 2017 as required to comply with Section 3 (8) (ii) (b) of the Banking Act Direction No. 11 of 2007 on Corporate Governance for Licensed Commercial Banks, issued by the Central Bank of Sri Lanka. This process assesses the adequacy and effectiveness of the internal controls and the processes for controlling business risks to ensure compliance with laws and regulations. The Committee ensures that appropriate action is taken by the management on the recommendations of the Internal Auditors to improve the effectiveness of the internal control system of the Bank. The Board of Directors performs its responsibilities on the basis of the internal control framework, which enables the Board to pursue its functions and take necessary measures. The Board's statement on effectiveness of the Bank's internal control mechanism is published on pages 140 and 142.

Internal Audit

The Audit Committee ensures that the Internal Audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care. The Audit Charter authorises and guides the Head of Group Internal Audit (HGIA) in carrying out the independent audit function of the Bank and its subsidiaries. The HGIA enjoys operational independence in conducting duties and has the authority to initiate, carry out and report on any action, which is considered necessary. For the performance of duties, the HGIA and audit staff shall have unrestricted, unlimited, direct and prompt access to all records of the Bank and subsidiaries, officials or personnel holding any contractual status of the Bank and subsidiaries, and to all the premises of the Bank and subsidiaries. The Audit Committee monitored and reviewed the scope, resources, extent and effectiveness of the activities of the Bank's Internal Audit Department.

With the concurrence of the Board of Directors, the Audit Committee engaged the services of two firms of Chartered Accountants to supplement the Bank's Internal Audit function in carrying out periodic audits at certain branches and few other assignments for the period ended 31 December 2017. The outsourced Internal Audit function is supervised by the HGIA of the Bank.

The Committee reviewed the progress of the risk based audits carried out in accordance with the Internal Audit plan approved by the Committee for the year 2017. During the year, the Internal Audit Department has reviewed business lines, critical operational processes, risk and compliance functions, branches and subsidiary operations. Further, the Department has conducted thematic audits focusing on particular audit objective across the audited units/branches. The Potential Fraud Monitoring Unit under Internal Audit carries out testing and data analytics related to potential fraud risk areas on a continuous basis.

The Internal Audit Department suggested simplified and efficient business processes where it was deemed necessary. In 2017, the Board Audit Committee reviewed audit reports of branches and departments, IS Audits, Thematic Audits and special investigations of the Bank. The Committee reviewed the Internal Audit reports of the Bank's subsidiaries as well.

The Committee had necessary interactions with the HGIA throughout the year. The Board Audit Committee advised Corporate Management to take precautionary measures on significant audit findings. The Committee reviewed the structure, resources and performance of the Bank's Internal Audit Department at the year end.

External Audit

The Committee reviewed and monitored the External Auditors' independence and objectivity and the effectiveness of the audit process, taking into consideration relevant professional and regulatory requirements. The Committee approved the policy in place on non-audit services provided by the External Auditors.

The Committee discussed with the Auditors their audit plan, scope and the methodology they propose to adopt in conducting the annual audit prior to its commencement. The Auditors were also provided with opportunities to meet the Audit Committee separately, without the presence of executive management, to ensure that the Auditors had the independence to discuss and express their opinions on any matter. There was no limitation of scope and the management has fully provided all information and explanations requested by the Auditors. The Committee also met the Auditors to review the management letter with the responses from the management.

The Audit Committee has recommended to the Board of Directors that, KPMG Chartered Accountants, be reappointed for the financial year ending 31 December 2018 subject to the approval of shareholders at the next Annual General Meeting.

Whistleblowing Policy

The Whistleblowing Policy of the Bank and its subsidiaries was reviewed and recommended by the Audit Committee during the year 2017 in order to further strengthen the policy as a communication channel to raise any genuine concerns. The Committee continuously emphasised on sustaining ethical conduct amongst staff members. In this regard, a Code of Ethics and Whistleblowing Policy was put in place and all members of staff were educated and encouraged to practice whistle blowing if they suspect any wrong doing. All appropriate procedures and techniques are in place to conduct independent investigations into incidents reported through whistle blowing or identified through other channels. The Whistleblowing Policy guarantees the maintenance of strict confidentiality of the identity of the whistle blowers. The Policy is subject to annual review in order to further improve its effectiveness.

Evaluation

The effectiveness of the Committee is self-evaluated annually by its members. An independent evaluation of the effectiveness of the Committee was carried out by the other members of the Board and the Committee has been found to be effective.

P M B Fernando

Chairman – Audit Committee

19 February 2018

Report of the Human Resources and Remuneration Committee

The Composition

The Human Resources and Remuneration Committee appointed by the Board of Directors, presently consists of three Non-Executive Directors. C R Jansz is the Chairman of the Committee. K P Cooray and Ms S R Thambiayah, are the other members. Ms V J Senaratne also functioned as a member of the Committee until April 2017.

The Chief Executive Officer attended meetings by invitation and participated in its deliberations except when his own evaluation and remuneration was under discussion. He also serves as the Secretary. The Group Vice President Human Resources assisted the Committee, by providing relevant information. The Committee, obtains input from external specialists as and when required.

The Mandate

Terms of Reference of the Committee adopted by the Board encompasses the tasks specified in Section 3 (6) (iii) of Direction No. 11 of 2007 of the Central Bank of Sri Lanka on Corporate Governance for Licensed Commercial Banks.

The Committee, in determining the Remuneration Policy relating to Directors, Chief Executive Officer and Key Management Personnel of DFCC Bank in terms of Directions, ensures appropriate compensation levels in order to attract, retain and motivate talented staff with the core capabilities matched to its strategy, and also to ensure that the Bank consistently delivers value to all stakeholders and to make the Organisation more competitive. To achieve this, the Committee uses a mixture of fixed and variable pay to reward employees. During the year under review, the Committee oversaw a review of the remuneration structure based on a comprehensive remuneration survey carried out by a firm of external consultants among comparable institutions.

The Procedure

Apart from the general review of remuneration, in keeping with the policy of pay for performance, the Committee reviewed the performance of the Bank against the historical performance, key performance indicators agreed at the beginning of the year as well as against a peer group when determining and recommending to the Board the annual salary increment pool and the performance based variable pay pool for DFCC Bank. The Committee also appraised the performance of the Chief Executive Officer based on the pre-agreed targets and desired skills and reviewed his remuneration.

In addition, the Committee considers and recommends to the Board of Directors from time to time, the requirements of additional/new expertise/skills and also salary revisions. The Committee periodically assesses the succession plan for key management positions and took appropriate steps to induct external skills to strengthen the Management of the Bank where it was deemed necessary.

Meetings

The Committee held eight meetings during the financial year to carry out its task. The attendance by members is given on page 113 of this Annual Report.

C R Jansz
Chairman – Human Resources and Remuneration Committee

19 February 2018

Report of the Nomination and Governance Committee

Composition

The Nomination and Governance Committee of the Board of Directors consists of three Non-Executive Directors. P M B Fernando an Independent Director is the Chairman with Messrs C R Jansz and K P Cooray serving as members.

The Chief Executive Officer attends the meeting by invitation, while the Secretary to the Board functions as the Secretary of the Committee.

Mandate

During the year under review, the Committee carried out the tasks as set out in the Terms of Reference approved by the Board. The Terms of Reference approved by the Board encompasses the tasks set out in Section 3 (6) (iii) of Direction No. 11 of 2007 of the Central Bank of Sri Lanka on Corporate Governance in Licensed Commercial Banks.

In terms of the mandate the role of the Committee is to review governance policies and procedures, evaluate the performance of the Board, and identify and evaluate persons with the required skills, knowledge, standing, fitness and propriety to join the Board of the Bank and to evaluate the suitability of Directors who are seeking re-election. The Committee is also responsible for the task of implementing a procedure for the appointment of the CEO and Key Management Personnel.

Procedure

The Committee meets when required and acts within its mandate approved by the Board of Directors and makes recommendations to the Board for consideration.

Meetings

Six meetings were held during the year. The Committee considered and recommended to the Board, the appointment of two new Directors. The Committee identified persons to fill key management positions interviewing many candidates from time to time to ascertain the best fit for the Bank, in terms of qualifications, ability and character, and reviewed succession planning and assessed the fitness and propriety of Directors and Key Management Personnel, in terms of the requirements of the Banking Act. In order to improve the process for succession planning for KMPs, a committee was formed comprising a member of the Audit Committee, CEO, and Head of HR.

The Committee reviewed the Job Descriptions (JDs) of Key Management Personnel and incorporated necessary changes to the JDs of the respective KMPs. In addition to the annual evaluation of the Board carried out by the individual members, this year, an evaluation of the Board was also carried out by the Nomination and Governance Committee members based on a separate check list approved by the Committee and the results were shared with the other members of the Board. During the year, the Committee also reviewed and updated the procedure for selection/appointment of Key Management Personnel.

Individual Committee members do not participate in discussions in matters relating to them. The attendance by Directors at meetings is given on page 113 of the Annual Report. The Committee has recommended the re-election of the Directors offering themselves for re-election at the Annual General Meeting.

P M B Fernando

Chairman – Nomination and Governance Committee

19 February 2018

Report of the Board Integrated Risk Management Committee

Composition of Board Integrated Risk Management Committee (BIRMC)

During the financial year ended December 2017, the composition of Board Integrated Risk Management Committee (BIRMC) of DFCC Bank was changed with the change of Chairman and the other Non-Executive Directors due to the retirement of some of the Directors and as recommended by the Board of Directors. L N de S Wijeyeratne (Non-Executive Director of DFCC Bank), the Chairman of BIRMC, on his retirement handed over the responsibilities to T Dharmarajah (Non-Executive Director of DFCC Bank), appointing him as the new Chairman of the Committee from November 2017. Further, Ms V J Senaratne and Ms L K A H Fernando were appointed as members representing Non-Executive Directors, while K D N R Asoka and P M B Fernando retired from the membership during the year. H A Ariyaratne was in membership for the first meeting in 2017.

There are three Non-Executive Directors and an Executive Director as at 31 December 2017. The Group Chief Risk Officer, who has the voting power, functions as the Secretary to the Committee. Heads of key functional areas such as Lending, Finance, Treasury, Operations, Information Technology, Internal Audit, and Compliance attend the meetings on invitation. The membership of the BIRMC as at 31 December 2017 was as follows:

- T Dharmarajah – Chairman of the Committee/ Non-Executive Director of DFCC Bank
- L H A L Silva – Executive Director/Chief Executive Officer of DFCC Bank
- Ms V J Senaratne – Non-Executive Director of DFCC Bank
- Ms L K A H Fernando – Non-Executive Director of DFCC Bank
- P Gamage – Group Chief Risk Officer

Charter and the Responsibilities of the BIRMC

The approved Charter for the BIRMC stipulates authority, structure, responsibilities, and tasks of BIRMC. As per its Charter, the primary responsibilities of BIRMC are to review and ensure;

a. Integrity and adequacy of the risk management function of the Bank.

b. Adequacy of the Bank's capital and its allocation.

c. Risk exposures and risk profiles of DFCC Bank are within acceptable parameters and to make recommendations to the Board of Directors on any action required.

d. Review the adequacy and effectiveness of the Management Committees through a set of defined tools.

e. Availability of a comprehensive and updated set of risk policies and guidelines covering overall operations of the Group.

f. The compliance of the Group's operations with relevant laws, regulations, and standards including the adherence to the CBSL Direction on Corporate Governance.

The process through which the BIRMC discharges its responsibilities is detailed in the Risk Management section of this Annual Report.

BIRMC Meetings

BIRMC meets on a quarterly basis. Accordingly, DFCC Bank convened four BIRMC meetings during 2017. The attendance of members is listed on page 113 of this Annual Report. The Committee continued to review policy frameworks, risk management strategies, risk capital position and key risk indicators at these meetings and was satisfied that the risk exposures of the Bank and the Group were being appropriately managed. During the financial year, the following key initiatives were achieved by the Committee:

a. Reviewed and approved the Internal Capital Adequacy Assessment Process (ICAAP) of DFCC Bank, which was a regulatory requirement with effect from January 2014. BIRMC took several key decisions on the capital management based on the outcome revealed by the ICAAP. They included taking steps to enhance retained earnings by considering options such as reducing dividend payout and issuing scrip dividends. However, ICAAP did not indicate any additional capital infusion requirement for 2017. BIRMC will continue monitoring and proposing future capital requirements as per the Bank's growth targets for the next few years.

b. In relation to the management of compliance risk, compliance risk indicators with different risk scales were reviewed and specific areas of focus were recognised based on the possible impact and the probability of occurrence.

c. Risk controls and monitoring tools were further improved with revisions to the overall risk limits system of the Bank from time to time as required.

d. The Committee approved the revisions of credit rating models for corporate exposures subsequent to an external validation of the model. This revision focused on recognising the borrower risk profile in a better approach and reducing the subjectivity in assigning the scores for the model parameters. These changes have been implemented in the Bank during the year. Further, the Committee approved a new rating model for the retail exposures as well.

e. The Committee reviewed the Probability of Default (PD) based on the rating grades, Loss Given Default (LGD) for facilities and technical validation results for the credit rating models. These credit risk parameters are used in credit appraisal process, credit pricing and risk management.

f. The annual review of effectiveness and adequacy of the Management Committees, was conducted by the BIRMC during the first quarter of 2017. The review results were shared with the respective committees for necessary improvements.

g. Reviewed and approved certain new products and redesign of certain existing products of the Bank while taking both business and risk management perspective.

h. Reviewed the CBSL recommendations based on the examination report requirements in relation to the integrated risk management function of the Bank.

i. Having duly recognised the trends in increasing threats on systems and information security, the committee paid increased attention by reviewing the adequacy of the security in information systems and closely monitoring the action plans and implementation of new projects for further improving information systems security in the Bank.

Several new risk management policies and guidelines were introduced during the financial year, while all existing risk policies and practices were reviewed by the Committee in line with the Bank specific requirements, industry dynamics, and regulatory specifications.

Reporting

The proceedings of the BIRMC meetings are reported to the Board through submission of the meeting minutes. Top and Emerging Risks and other specific matters are submitted separately for the Board's approval. The recommendations made by the BIRMC during the year under review were approved by the Board.

T Dharmarajah

Chairman – Board Integrated Risk Management Committee

19 February 2018

Report of the Credit Approval Committee

The Composition

The Credit Approval Committee of the Board of Directors presently consists of three Non-Executive Directors. C R Jansz is the Chairman with Messrs P M B Fernando and K P Cooray serving as members.

T Dharmarajah also functioned as a member of the Committee until 31 October 2017.

The Company Secretary functions as the Secretary of the Committee.

The Mandate

The Committee carried out the tasks set out in the Terms of Reference approved by the Board. The primary purpose of the Committee is to review and where appropriate, recommend or approve credit facilities which require approval above the delegated limit of the Management Credit Committee of the Bank.

The Procedure

The Committee meets at least once a month and as and when required. The Committee invites the relevant officers to these meetings to clarify issues and for discussion relating to proposals that are submitted for review and also guides the management in improving the credit policies, and procedures, and on process improvements for monitoring and recovery action.

Meetings

The Committee held 13 meetings during the financial year to carry out its task. The attendance by members is given on page 113 of the Annual Report. The proceedings of the Committee meetings have been regularly reported to the Board of Directors. Credit facilities recommended by the Committee were submitted to the monthly meeting of the Board for approval.

C R Jansz

Chairman – Credit Approval Committee

19 February 2018

Report of the Related Party Transactions Review Committee

The Composition

The Related Party Transactions Review Committee appointed by the Board of Directors, presently consists of three Non-Executive Directors and the Chief Executive Officer. T Dharmarajah an Independent Director is the Chairman of the Committee. C R Jansz, K P Cooray and L H A L Silva are the other members. A R Fernando functioned as a member of the Committee until his retirement in August 2017.

The Company Secretary functions and the Secretary of the Committee.

The Mandate

The Committee adopted as its mandate, the tasks specified in Section 9 of the Colombo Stock Exchange (CSE) Listing Rules. The Terms of Reference of the Committee has been formally adopted by the Board.

The primary purpose of the Committee is to evaluate and consider all transactions with related parties of the Bank except the exempted transactions as set out in Rule 9.5 of the Listing Rules of the CSE, in order to ensure that transactions with related parties are on normal commercial terms similar to those afforded to non-related parties.

The Procedure

The Committee meets as and when required and at least once in a calendar quarter and makes recommendations to the Board for consideration.

The Committee has put in place the necessary processes to identify, review, disclose and monitor related party transactions according to the provisions contained in the Board approved Related Party Transactions Policy of the Bank.

The Bank obtains on a quarterly basis, a declaration from all Key Management Personnel on a structured format to assist in the process of collating related party transactions. Relevant officers are informed of the applicable regulatory requirement relating to Related Party Transactions and have been advised to submit a report on the prescribed format for transactions that require a review by the Committee.

Meetings

The Committee held 12 meetings during the financial year to carry out its task. The attendance by members is given on page 113 of the Annual Report. The proceedings of the Committee meetings have been regularly reported to the Board of Directors.

T Dharmarajah
Chairman – Related Party Transactions Review Committee

19 February 2018

Directors' Statement on Internal Control

Introduction

Section 3 (8) (ii) (b) of the Banking Act Direction No. 11 of 2007 requires the Board of Directors ('the Board') to report on the internal control mechanism that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of Financial Statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements. This report is to be in line with the said regulatory requirement.

Internal Control System

The internal control system is the process designed and effected by those charged with governance, management and other personnel, to provide reasonable assurance about the achievement of DFCC Bank PLC's ('the Bank') objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

The internal control system of the Bank consists of the following components:

a. The control environment;

b. The entity's risk assessment process;

c. The information system, including the related business processes, relevant to financial reporting and communication;

d. Control activities; and

e. Monitoring of controls.

The subset of this wider internal control system is the internal controls designed and implemented to provide reasonable assurance regarding the reliability of the financial reporting, and that the preparation of Financial Statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.

Responsibility

The Board acknowledges the responsibility for the adequacy and effectiveness of the Bank's system of internal controls, which is designed to provide assurance on the maintenance of proper accounting records and the reliability of financial information generated, and safeguarding of the assets of the Bank. However, such systems are designed to manage the Bank's key exposures to risk within acceptable risk parameters, rather than to eliminate the risk of failure to achieve the business goals and objectives of the Bank. Therefore, the system of internal controls can only provide reasonable and not absolute assurance against errors or material misstatement of management and financial information and records, or against financial losses or fraud.

Framework for Managing Material Risks of the Bank

The Board has set-up an ongoing process for identifying, monitoring and managing the material risks faced by the Bank. This includes establishment of a dedicated Risk Management Department that provides regular reports on various risks, subject to an oversight by the Internal Audit Department through Internal Audit Reports, that enables the Audit Committee to review the adequacy and effectiveness of the system of internal controls continuously to match the changes in the business environment or regulatory guidelines. In making this assessment, all key processes relating to material or significant transactions captured and recorded in the books of accounts are identified and covered on an ongoing basis that is compatible with the guidance for Directors of Banks on the Directors' Statement of Internal Control issued by The Institute of Chartered Accountants of Sri Lanka.

Key Internal Control Processes

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

- The Board has established Committees to assist them in exercising oversight on the effectiveness of the Bank's daily operations and ensuring that they are in accordance with the corporate objectives, strategies and the budgetary targets as well as the policies and business directions that have been approved.
- The Internal Audit Department of the Bank verifies compliance of operations with policies and procedures and the adequacy and effectiveness of the internal control systems, and highlights significant findings in respect of any non-compliance. Audits are carried out on all units 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 Bank reviews internal control issues identified by the internal audit, the External Auditors, regulatory authorities and management, and evaluates the adequacy and effectiveness of the risk management and internal control systems. They also review the internal audit function focusing on the scope of audits and the quality of reporting. The minutes of the Audit Committee meetings are tabled for the information of the Board on a periodic basis. Further, details of the activities undertaken by the Audit Committee of the Bank are set out in the Report of the Audit Committee on page 131.
- The Board Integrated Risk Management Committee (BIRMC) was established by the Board to assist the Board to oversee the overall management of principal areas of risk of the Bank. The BIRMC includes representation from all key business and operational areas of the Bank, and the Board is assisted in the implementation of policies, procedures and controls identified by the BIRMC.
- Operational Committees have also been established with appropriate mandates to ensure effective management and supervision of the Bank's core areas of business operations. These Committees include the Management Committee, Credit Committees, the Asset/Liability Committee, the Impairment Assessment Committee and the Information Technology Steering Committee.

Assessment of the Adequacy and Effectiveness of Internal Control

Although this process is carried out every year on a continuous basis, the Direction on Corporate Governance issued by the Central Bank of Sri Lanka requires the Board to provide a separate report on the Bank's Internal Control mechanism, that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of Financial Statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements, supplemented with independent certification by the Auditor. The Auditors provide the Independent Assurance Report in accordance with Sri Lanka Standard on Assurance Engagements (SLSAE) – 3050 issued by The Institute of Chartered Accountants of Sri Lanka.

In order to facilitate the tasks of the Auditors to issue the Independent Assurance Report, the SLSAE – 3050 requires documentation of all procedures and controls that are related to significant accounts and disclosures of the Financial Statements of the Bank, with audit evidence of checks performed by the Bank on an ongoing basis.

The risk and significance based Internal Audit Plan implemented by the Internal Audit Department in consultation with the Board Audit Committee, specifically included on a sample basis, independent verification that the internal control process documented by the Bank, which is supported with audit evidence, was in fact carried out on an ongoing basis.

Transition to New Sri Lanka Accounting Standards

Consequent to full convergence of Sri Lanka Accounting Standards with International Financial Reporting Standards and International Accounting Standards that became effective from 2012, the Bank implemented a process to ensure changes arising from new accounting standards are adequately identified, recognised and disclosed in the Financial Statements. The process for making necessary adjustments based on Sri Lanka Accounting Standards – LKAS 39 continue to be made based on excel software application, for which the feasibility of developing or acquiring a separate system is currently being evaluated. The process followed by the Bank for quantification of adjustments is continuously reviewed and further improvements were made during the current year. The testing of such processes by the internal audit was carried out during the year. These processes will be further improved on an ongoing basis.

The Board also has taken into consideration the requirements of "SLFRS 09 - Financial Instruments" accounting standard which is to be effective from 01 January 2018, as it is expected to have significant impact on the calculation of impairment on financial instruments of the Bank. The impact assessment on transition to SLFRS 09 has been completed based on data compiled up to 31 December 2016 with the assistance of an external consultant. The same impact assessment is further extended to include data up to 31 December 2017 which is currently underway. A separate note on the implementation of SLFRS 09 and its impact to the financial statements is given under the Explanatory Note No. 8.1.1 in page 171.

The computation of impairment losses from Loans and Advances has not been automated yet. Considering the complexity and level of estimation involved in this process, the Board is evaluating the options available for automation. This evaluation process will also address the new parameter requirements which will become applicable with the adoption of SFLRS 9.

Management Information

The comments made by the External Auditors in connection with the internal control system for the financial year ended 31 December 2016 were reviewed during the year and appropriate steps have been taken to rectify them.

The recommendations made by the External Auditor in the financial year ended 31 December 2017 in connection with the internal control system will be addressed in future.

The Directors are of the opinion that these recommendations are intended to further improve the internal control system and they do not in any way detract from the conclusion that the financial reporting system is reliable to provide reasonable assurance, that the Financial Statements for external use are true and fair and complies with Sri Lanka Accounting Standards and the regulatory requirements of the Central Bank of Sri Lanka.

Confirmation

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

Review of the Statement by External Auditors

The External Auditors have reviewed the above Directors' Statement on Internal Control for the year ended 31 December 2017 and their Independent Assurance Report is on page 143 of the Annual Report.

By Order of the Board,

P M B Fernando
Chairman – Audit Committee

C R Jansz
Chairman – Board of Directors

L H A L Silva
Chief Executive Officer/Director

19 February 2018

Independent Assurance Report

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To the Board of Directors of DFCC Bank PLC

We were engaged by the Board of Directors of DFCC Bank PLC ("Bank") to provide assurance on the Directors' Statement on Internal Control ("Statement") included in the annual report for the year ended 31 December 2017.

Management's Responsibility for the Statement on Internal Control

Management is responsible for the preparation and presentation of the Statement in accordance with the "Guidance for Directors of Banks on the Directors' Statement on Internal Control" issued in compliance with the section 3(8)(ii)(b) of the Banking Act Direction No. 11 of 2007, by The Institute of Chartered Accountants of Sri Lanka.

Scope of the Engagement in Compliance with SLSAE 3050

Our responsibility is to issue a report to the Board on the Statement based on the work performed. We conducted our engagement in accordance with Sri Lanka Standard on Assurance Engagements SLSAE 3050 – Assurance Report for Banks on Directors' Statement on Internal Control issued by The Institute of Chartered Accountants of Sri Lanka.

Summary of Work Performed

Our engagement has been conducted to assess whether the Statement is both supported by the documentation prepared by or for directors and appropriately reflects the process the directors have adopted in reviewing the system of internal control for the Bank.

To achieve this objective, appropriate evidence has been obtained by performing the following procedures:

(a) Enquired the directors to obtain an understanding of the process defined by the Board of Directors for their review of the design and effectiveness of internal control and compared their understanding to the Statement made by the directors in the annual report.

(b) Reviewed the documentation prepared by the directors to support their Statement made.

(c) Related the Statement made by the directors to our knowledge of the Bank obtained during the audit of the financial statements.

(d) Reviewed the minutes of the meetings of the Board of Directors and of relevant Board Committees.

(e) Attended meetings of the audit committee at which the annual report, including the Statement on Internal Control is considered and approved for submission to the Board of Directors.

(f) Considered whether the Directors' Statement on Internal Control covers the year under review and that adequate processes are in place to identify any significant matters arising.

(g) Obtained written representations fr Image om directors on matters material to the Statement on Internal Control where other sufficient appropriate audit evidence cannot reasonably be expected to exist.

SLSAE 3050 does not require us to consider whether the Statement covers all risks and controls, or to form an opinion on the effectiveness of the Bank's risk and control procedures. SLSAE 3050 also does not require us to consider whether the processes described to deal with material internal control aspects of any significant problems disclosed in the annual report will, in fact, remedy the problems.

Our Conclusion

Based on the procedures performed, nothing has come to our attention that causes us to believe that the Statement included in the annual report is inconsistent with our understanding of the process the Board of Directors have adopted in the review of the design and effectiveness of internal control system over the financial reporting of the Bank.

Chartered Accountants
Colombo
19 February 2018

Investor Engagement

Listening to and maintaining a dialogue with the investors, both existing and potential, helps DFCC Bank to understand their expectations and concerns. Through this dialogue, the Bank fine-tunes engagement and structure reporting to be more relevant to them. This way, mutual trust and a loyal following of investors is built where they take a long-term view of the value of their investments in the Bank. Details about the frameworks that govern the Bank's engagement process and communication with investors can be found under Stakeholders, see page 31.

The CEO maintains a dialogue with key institutional investors and raises any matters of concern to the Board. The Board approved Communication Policy of the Bank ensures that information is made available to shareholders and other stakeholders through timely disclosures made to the CSE, publicity through press and electronic media, and posts on the Bank's website. The Annual General Meeting held on 30 March 2017 provided an opportunity for shareholders to interact with the Board and the Management.

Performance of the Share

The market value of the DFCC Bank PLC ordinary share on 31 December 2017 was LKR 122.80 compared to LKR 122.50 on 31 December 2016. During the 12 month period, the highest price of LKR 138.20 was recorded on 13 October 2017. The lowest price for the period was recorded on 28 March 2017 as LKR 110.00.

Share Information

DFCC Bank Share Price Information for the Period 1 January 2017 - 31 December 2017.

	01 January to 31 Decmber2017	01 January to 31 Decmber 2016
Price Indices		
ASPI	**6,369.26**	6,228.26
S&P SL20	**3,671.72**	3,496.44
Share Price		
Lowest Price (LKR)	**110.00**	116.8
Highest Price (LKR)	**138.20**	168.1
Closing Price (LKR)	**122.80**	122.5
Market Capitalisation		
Value (LKR million)	**32,554**	32,474
% of total market cap	**1.12**	1.18
Rank	**18**	18
Value of Shares Traded		
Value (LKR million)	**1,575.59**	1,308.91
% of total market turnover	**0.71**	0.73
Rank	**24**	29
Days Traded		
No. of days traded	**237**	240
Total no. of market days	**240**	240
% of market days traded	**98.75**	100
Frequency of Shares Traded		
No. of transactions	**5,350**	5,350
% of total frequency	**0.54**	0.51
Rank	**51**	60

Distribution of Shareholding

Categories of Shareholders

As at	31 December 2017			31 December 2016		
	Foreign	**Local**	**Total**	Foreign	Local	Total
Individual	**8.02**	**7.60**	**15.62**	5.76	8.35	14.11
Institutional	**15.89**	**68.49**	**84.38**	17.79	68.10	85.89
	23.91	**76.09**	**100.00**	23.55	76.45	100.00

Size-wise Distribution of Shareholding

Share range	31 December 2017			31 December 2016		
	Number of shareholders	**Total holding**	**%**	Number of shareholders	Total holding	%
01 – 1,000	**5,641**	**1,794,816**	**0.68**	5,630	1,817,586	0.69
1001 – 5,000	**2,362**	**4,865,268**	**1.84**	2,405	4,955,001	1.87
5,001 – 10,000	**322**	**2,328,317**	**0.88**	329	2,350,001	0.88
10,001 – 50,000	**293**	**6,448,247**	**2.43**	299	6,622,534	2.50
50,001 – 100,000	**41**	**2,963,550**	**1.12**	42	2,997,452	1.13
100,001 – 500,000	**44**	**9,155,740**	**3.45**	44	8,633,347	3.26
500,001 – 1,000,000	**3**	**1,987,718**	**0.75**	4	2,489,278	0.93
1,000,000 and above	**22**	**235,554,032**	**88.85**	23	235,232,489	88.74
	8,728	**265,097,688**	**100.00**	8,776	265,097,688	100.00

Public Holding as at 31 December 2017

Public holding percentage	63.4%
Number of public shareholders	8,715
Float adjusted market capitalisation	LKR 20,639 million
Applicable option as per CSE Listing Rule 7.13.1 (a)	Option 1

Twenty Major Shareholders of the Bank as at 31 December 2017

Name of Shareholder/Company	31 December 2017		31 December 2016*	
	No. of shares	**%**	No. of shares	%
Bank of Ceylon No. 2 A/c	**38,039,994**	**14.35**	38,039,994	14.35
Hatton National Bank PLC A/c No. 1	**32,396,140**	**12.22**	32,396,140	12.22
Sri Lanka Insurance Corporation Limited – LifeFund	**26,509,832**	**10.00**	26,509,832	10.00
Mr M A Yaseen	**26,296,700**	**9.92**	20,296,700	7.66
Employees' Provident Fund	**24,368,995**	**9.19**	24,368,995	9.19
Melstacorp PLC	**22,175,280**	**8.36**	22,175,280	8.36
Seafeld International Limited	**15,286,794**	**5.77**	15,286,794	5.77
HSBC Intl. Nom. Ltd. – BPSS Lux-Aberdeen Global Asia Pacific Equity Fund	**9,901,281**	**3.73**	12,216,146	4.61
Renuka City Hotels PLC	**6,926,870**	**2.61**	6,926,870	2.61
HSBC Intl. Nom. Ltd. – BP2S LDN-Aberdeen Asia Pacific Equity Fund	**5,470,928**	**2.06**	6,750,000	2.55
HSBC Intl. Nominees Ltd. – BP2S London-Edinburg Dragon Trust PLC	**4,555,187**	**1.72**	5,620,164	2.12
Renuka Hotels PLC	**4,073,360**	**1.54**	4,073,360	1.54
Employees' Trust Fund Board	**3,987,952**	**1.50**	3,987,952	1.50
HSBC Intl. Nominees Ltd. – BP2S London-Aberdeen Asia Smaller Companies Investment Trust	**3,889,870**	**1.47**	3,889,870	1.47
Akbar Brothers (Pvt) Ltd. A/c No. 1	**2,552,270**	**0.96**	1,255,747	0.47
Cargo Boat Development Company PLC	**2,498,200**	**0.94**	2,498,200	0.94
Anverally & Sons (Pvt) Ltd. A/c No. 1	**1,553,415**	**0.59**	1,528,395	0.58
Crescent Launderers & Dry Cleaners (Pvt) Ltd.	**1,482,548**	**0.56**	1,482,548	0.56
HSBC Intl. Nominees Ltd. – BP2S London-Aberdeen New Dawn Investment Trust XCC6	**1,458,914**	**0.55**	1,800,000	0.68
Renuka Consultants & Services Ltd	**1,097,992**	**0.41**	1,097,992	0.41
Total of the 20 major shareholders	**234,522,522**	**88.45**		
Other shareholders	**30,575,166**	**11.55**		
Total	**265,097,688**	**100.00**		

** Shareholding as at 31 December 2016 of the twenty largest shareholders as at 31 December 2017.*

Financial Reports

Financial Calendar – 2017

LKR 4.50 per share Final Dividend for 2016 paid on	13 March 2017
Audited financial statements signed on	19 February 2018
62nd Annual General Meeting to be held on	28 March 2018
LKR 5.00 per share Final Dividend for 2017 payable on	12 March 2018
1st Quarter Interim Results released on	3 May 2017
2nd Quarter Interim Results released on	31 July 2017
3rd Quarter Interim Results released on	6 November 2017

Proposed Financial Calendar – 2018

1st Quarter Interim Results to be released in	May 2018
2nd Quarter Interim Results to be released in	August 2018
3rd Quarter Interim Results to be released in	November 2018
63rd Annual General Meeting to be held in	March 2019

Statement of Directors' Responsibilities in Relation to Financial Statements

The Auditors' Report sets out the respective responsibilities of the Directors and Auditors relating to the financial statements and this statement provides additional information.

The Directors are required by relevant statutory provisions to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Bank and the Group for that period. The statutory provisions are in the Companies Act No. 07 of 2007, and Banking Act No. 30 of 1988, and amendments thereto. The application of principal qualitative characteristics and appropriate accounting standards and regulatory requirements inclusive of specific disclosures would result in financial statements that convey a true and fair view of financial information and financial position.

The Directors are satisfied that the Bank and Group have the resources to continue in business for the foreseeable future and therefore, these financial statements are prepared on a going concern basis.

The financial statements for the year ended 31 December 2017, and the comparative period have been prepared in accordance with Sri Lanka Accounting Standards (SLFRS and LKAS).

The Directors are responsible for keeping proper accounting records and to take reasonable steps as far as practicable, to ensure the accuracy and reliability of accounting records, to enable the preparation of financial statements. The Directors have a general responsibility to take reasonable steps to safeguard the assets of the Bank. In discharging these responsibilities, the Directors have instituted a system of internal financial controls and a system for monitoring its effectiveness. These provide reasonable but not absolute assurance of safeguarding of the Bank's assets, maintenance of proper accounting records and the reliability of financial information.

The Board appointed Audit Committee chaired by an Independent Non-Executive Director who possesses qualifications and experience in accountancy and audit assists the Directors to discharge their responsibility on the integrity of financial reporting system and monitoring the effectiveness and adequacy of internal control system. This Committee has made an independent assessment of the financial reporting system of the Bank and confirmed that to the best of its knowledge and belief the financial statements issued for external purposes by the Bank complied with Sri Lanka Accounting Standards and complies with the statutory provisions of the Companies Act No. 07 of 2007, and Banking Act No. 30 of 1988, as amended. The Report of The Audit Committee is on pages 131 to 133.

The Directors are in agreement with the assessment of the Audit Committee on the reliability of financial reporting system of the Bank and confirm that the financial statements prepared for external use is in accordance with relevant accounting principles and regulatory requirements. As part of institutional checks and balances and accountability, in addition to this Statement of Directors' Responsibilities in Relation to Financial Statements, the Directors have included the Chief Executive's and Chief Financial Officer's Statement of Responsibility on page 150.

By Order of the Board,

Ms A Withana
Company Secretary
Colombo
19 *February 2018*

Chief Executive's and Chief Financial Officer's Statement of Responsibility

The financial statements of DFCC Bank PLC ("the Bank") and the consolidated financial statements of the Bank and its subsidiaries as at 31 December 2017 are prepared and presented in compliance with the requirements of the following:

- Sri Lanka Accounting Standards issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka),
- Companies Act No. 07 of 2007,
- Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995,
- Banking Act No. 30 of 1988 (as amended),
- Listing Rules of the Colombo Stock Exchange,
- Banking Act Direction No. 11 of 2007 on Corporate Governance for Licensed Commercial Banks in Sri Lanka (as amended from time to time) and
- Code of Best Practice on Corporate Governance issued jointly by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka) and the Securities and Exchange Commission of Sri Lanka.

The formats used in the preparation of the financial statements and disclosures made comply with the formats prescribed by the Central Bank of Sri Lanka.

Financial statements are prepared in compliance with the Sri Lanka Financial Reporting Standards (SLFRS) issued by the Institute of Chartered Accountants of Sri Lanka, Companies Act No. 07 of 2007 and Banking Act No. 30 of 1988 as amended and Directions issued there under relating to financial statements formats and disclosure of information.

The Accounting Policies used in the preparation of the financial statements are appropriate and are consistently applied by the Group. There are no departures from the prescribed Accounting Standards in their adoption. Comparative information has been reclassified wherever necessary to comply with the current presentation. The Board of Directors and the Management of the Bank accept responsibility for the integrity and objectivity of these financial statements. The estimates and judgements relating to the financial statements were made on a prudent and reasonable basis, in order that the financial statements reflect true and fair view. To ensure this, the Bank has taken proper and sufficient care in installing a system of internal control and accounting records, for safeguarding assets and for preventing and detecting frauds as well as other irregularities, which is reviewed, evaluated and updated on an ongoing basis.

The Board of Directors assessed the effectiveness of the Bank's internal controls over financial reporting during the year ended 31 December 2017, as required by the Banking Act Direction No. 11 of 2007, result of which is given on page 140 to 142 in the Annual Report, the "Directors' Statement on Internal Control". External auditor's Independent Assurance Report on the "Directors' Statement on Internal Control" is given on page 143 of the Annual Report.

It is confirmed that the Bank has adequate resources to continue its operations in the foreseeable future. Therefore, the Bank will continue to adopt the "going concern" basis in preparing these financial statements.

Bank's internal auditors have conducted periodic audits to provide reasonable assurance that the established policies and procedures of the Bank were consistently followed. However, there are inherent limitations that should be recognised in weighing the assurances provided by any system of internal controls and accounting.

The financial statements of the Group were audited by Messrs KPMG. The Joint Venture company Acuity Partners (Pvt) Ltd and the Associate company National Asset Management Limited, are also audited by Messrs KPMG.

The Audit Committee of the Bank meets periodically with the internal auditors and the independent auditors to review the manner in which the external auditor performs their responsibilities, and to discuss auditing, internal control and financial reporting issues. To ensure complete independence, the independent auditor and the internal auditors have full and free access to the members of the Audit Committee to discuss any matter of substance. Details of which are given in the "Audit Committee Report" on pages 131 to 133 .

The Audit Committee approves the audit and non-audit services provided by external auditor, Messrs KPMG, in order to ensure that the provision of such services does not impair KPMG's independence.

We confirm that,

- the Bank and its subsidiaries have complied with all applicable laws, regulations and prudential requirements;
- there are no material non compliances; and
- there are no material litigations that are pending against the Group other than those disclosed in the Note 54.2 to the financial statements in this Annual Report.

L H A L Silva
Director/Chief Executive Officer

Ashok Goonesekere
Chief Financial Officer

Colombo

19 February 2018

Independent Auditors' Report

KPMG

KPMG
(Chartered Accountants)
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TO THE SHAREHOLDERS OF DFCC BANK PLC

Report on the Financial Statements

We have audited the accompanying financial statements of DFCC Bank PLC, ("the Bank"), and the consolidated financial statements of the Bank and its subsidiaries ("Group"), which comprise the statement of financial position as at December 31, 2017, income statement, statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information set out on pages 152 to 244 of the annual report.

Board's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, 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 entity's preparation of the financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Board, as well as evaluating the overall presentation of the financial statements.

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

Opinion

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

Report on Other Legal and Regulatory Requirements

As required by section 163 (2) of the Companies Act No. 07 of 2007, we state the following:

a) The basis of opinion and scope and limitations of the audit are as stated above.

b) In our opinion:

   — We have obtained all the information and explanations that were required for the audit and, as far as appears from our examination, proper accounting records have been kept by the Bank.

   – The Financial Statements of the Bank give a true and fair view of its financial position as at December 31, 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 Bank and the Group, comply with the requirements of sections 151 and 153 of the Companies Act No. 07 of 2007.

KPMG

CHARTERED ACCOUNTANTS

19 February 2018

Colombo, Sri Lanka

Income Statement

For the year ended 31 December	Notes	Page No.	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Income	9	172	**35,941,612**	26,753,895	**35,987,091**	26,980,083
Interest income			**32,986,590**	24,194,158	**32,994,636**	24,206,112
Interest expenses			**21,643,982**	15,293,022	**21,597,373**	15,262,906
Net interest income	10	172	**11,342,608**	8,901,136	**11,397,263**	8,943,206
Fee and commission income			**1,591,336**	1,309,049	**1,591,943**	1,309,049
Fee and commission expenses			**–**	–	**–**	–
Net fee and commission income	11	173	**1,591,336**	1,309,049	**1,591,943**	1,309,049
Net gain from trading	12	174	**361,647**	340,456	**361,647**	340,456
Net loss from financial instruments at fair value through profit or loss	13	174	**(404,586)**	(179,727)	**(404,586)**	(179,727)
Net gain from financial investments	14	175	**2,238,166**	1,165,389	**1,945,118**	1,081,129
Other operating (loss)/income – net	15	175	**(831,541)**	(75,430)	**(501,667)**	223,064
Total operating income			**14,297,630**	11,460,873	**14,389,718**	11,717,177
Impairment for loans and other losses	16	176	**1,176,413**	937,267	**1,170,366**	916,344
Net operating income			**13,121,217**	10,523,606	**13,219,352**	10,800,833
Operating expenses						
Personnel expenses	17	177	**3,166,509**	2,809,742	**3,302,793**	2,980,069
Other expenses	18	180	**2,703,646**	2,314,224	**2,751,430**	2,321,637
Operating profit before value added tax and nation building tax on financial services			**7,251,062**	5,399,640	**7,165,129**	5,499,127
Value added tax and nation building tax on financial services	19	180	**1,458,749**	986,110	**1,458,749**	986,110
Operating profit after value added tax and nation building tax on financial services			**5,792,313**	4,413,530	**5,706,380**	4,513,017
Share of profits of associate and joint venture			**–**	–	**185,030**	161,151
Profit before income tax			**5,792,313**	4,413,530	**5,891,410**	4,674,168
Income tax expense	20	181	**1,377,349**	1,124,807	**1,457,653**	1,205,094
Profit for the year			**4,414,964**	3,288,723	**4,433,757**	3,469,074
Profit attributable to:						
Equity holders of the Bank			**4,414,964**	3,288,723	**4,362,407**	3,414,980
Non-controlling interests			**–**	–	**71,350**	54,094
Profit for the year			**4,414,964**	3,288,723	**4,433,757**	3,469,074
Basic earnings per ordinary share (LKR)	21	182	**16.65**	12.41	**16.45**	12.88

Notes to the financial statements from pages 161 to 244 form part of these financial statements.

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Profit for the year	**4,414,964**	3,288,723	**4,433,757**	3,469,074
Other comprehensive income/(expenses) for the year, net of tax				
Items that are or may be reclassified subsequently to income statement				
Available-for-sale financial assets:				
Net change in fair value of available-for-sale financial assets	**206,651**	206,916	**206,651**	206,916
Net amount transferred to income statement on disposal of available-for-sale financial assets	**(1,188,907)**	(8,533)	**(987,323)**	(8,533)
Tax expense relating to available-for-sale financial assets	**(268,545)**	65,447	**(268,545)**	65,447
Share of other comprehensive expenses of equity accounted joint venture	**–**	–	**(22,136)**	(21,154)
Share of other comprehensive income/(expenses) of equity accounted associate	**–**	–	**479**	(3,359)
Total other comprehensive (expenses)/income that are or may be reclassified subsequently to income statement	**(1,250,801)**	263,830	**(1,070,874)**	239,317
Items that will not to be reclassified to income statement				
Actuarial gains and losses on defined benefit plans	**32,399**	137,764	**36,411**	140,509
Tax expense relating to actuarial gains and losses on defined benefit plans	**2,600**	3,082	**2,028**	2,844
Total other comprehensive income not to be reclassified to income statement	**34,999**	140,846	**38,439**	143,353
Other comprehensive (expenses)/income for the year, net of tax	**(1,215,802)**	404,676	**(1,032,435)**	382,670
Total comprehensive income for the year	**3,199,162**	3,693,399	**3,401,322**	3,851,744
Total comprehensive income attributable to:				
Equity holders of the Bank	**3,199,162**	3,693,399	**3,329,750**	3,797,474
Non-Controlling interests	**–**	–	**71,572**	54,270
Total comprehensive income for the year	**3,199,162**	3,693,399	**3,401,322**	3,851,744

Notes to the financial statements from pages 161 to 244 form part of these financial statements.

Statement of Financial Position

As at	Notes	Page No.	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Assets						
Cash and cash equivalents	24	186	**4,106,225**	4,330,934	**4,120,230**	4,344,260
Balances with Central Bank of Sri Lanka	25	187	**10,557,688**	8,062,567	**10,557,688**	8,062,567
Placements with banks	26	187	**6,691,381**	1,351,117	**6,712,131**	1,415,985
Derivative assets held-for-risk management	27	187	**66,440**	122,977	**66,440**	122,977
Other financial assets held-for-trading	28	188	**310,922**	–	**310,922**	–
Loans to and receivables from banks	29	189	**10,984,266**	12,300,398	**10,984,266**	12,300,398
Loans to and receivables from other customers	30	190	**213,675,866**	185,784,979	**213,675,866**	185,784,979
Financial investments – available for sale	31	192	**56,866,054**	49,272,243	**56,866,054**	49,272,243
Financial investments – held to maturity	32	197	**23,507,632**	23,189,085	**23,507,632**	23,189,085
Investments in subsidiaries	33	198	**167,036**	111,932	**–**	–
Investments in associate	34	199	**35,270**	35,270	**67,266**	64,873
Investments in joint venture	35	200	**755,000**	755,000	**1,616,711**	1,378,254
Due from subsidiaries	36	201	**12,083**	19,855	**–**	–
Investment property	37	201	**–**	–	**318,653**	231,352
Property, plant and equipment	38	202	**1,273,250**	927,857	**1,371,161**	1,042,619
Intangible assets	39	204	**498,084**	203,742	**502,411**	208,382
Goodwill on consolidation	40	205	**–**	–	**156,226**	156,226
Government grant receivable	41	206	**642,583**	861,915	**642,583**	861,915
Deferred tax asset	42	207	**–**	–	**3,160**	628
Other assets	43	209	**2,957,562**	2,730,999	**2,988,462**	2,777,676
Total assets			**333,107,342**	290,060,870	**334,467,862**	291,214,419
Liabilities						
Due to banks	44	209	**9,640,735**	18,103,587	**9,640,735**	18,103,587
Derivative liabilities held-for-risk – management	27	187	**367,435**	105,741	**367,435**	105,741
Due to other customers	45	209	**193,307,534**	140,514,373	**192,920,147**	140,219,872
Other borrowing	46	209	**41,319,591**	40,751,346	**41,290,874**	40,736,300
Debt securities issued	47	210	**24,443,767**	29,179,185	**24,443,767**	29,179,185
Current tax liability			**633,636**	607,333	**655,488**	626,470
Deferred tax liability	42	207	**1,194,027**	851,662	**1,232,478**	873,912
Government grant – deferred income	41	206	**654,583**	701,665	**654,583**	701,665
Other liabilities	48	211	**4,466,398**	4,190,675	**4,657,628**	4,352,331
Subordinated term debt	49	216	**9,202,870**	9,205,637	**9,202,870**	9,205,637
Total liabilities			**285,230,576**	244,211,204	**285,066,005**	244,104,700

As at	Notes	Page No.	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Equity						
Stated capital	50	216	**4,715,814**	4,715,814	**4,715,814**	4,715,814
Statutory reserve	51	217	**2,224,275**	2,004,275	**2,224,275**	2,004,275
Retained earnings	52	217	**13,858,152**	10,800,251	**17,359,593**	14,231,009
Other reserves	53	217	**27,078,525**	28,329,326	**24,825,383**	25,898,721
Total equity attributable to equity holders of the Bank			**47,876,766**	45,849,666	**49,124,985**	46,849,819
Non-controlling interests			**–**	–	**276,872**	259,900
Total equity			**47,876,766**	45,849,666	**49,401,857**	47,109,719
Total equity and liabilities			**333,107,342**	290,060,870	**334,467,862**	291,214,419
Contingent liabilities and commitments	54	217	**135,571,324**	101,452,101	**135,571,324**	101,452,101
Net assets value per share, LKR			**180.60**	172.95	**185.31**	176.73

The notes to the financial statements from pages 161 to 244 form part of these financial statements.

I certify that these financial statements comply with the requirements of the Companies Act, No. 07 of 2007.

Ashok Goonesekere
Chief Financial Officer

For and on behalf of the Board of Directors,

C R Jansz
Chairman
Colombo

L H A L Silva
Director and Chief Executive

19 February 2018

Statement of Changes in Equity

		Statutory reserves	Other reserves			
	Stated capital LKR 000	Reserve fund LKR 000	Fair value reserve LKR 000	General reserve LKR 000	Retained earnings LKR 000	Total equity LKR 000
Bank						
Balance as at 31.12.2015	4,715,814	1,834,275	14,285,657	13,779,839	8,203,426	42,819,011
Profit for the year	–	–	–	–	3,288,723	3,288,723
Other comprehensive income net of tax	–	–	263,830	–	140,846	404,676
Total comprehensive income for the year	–	–	263,830	–	3,429,569	3,693,399
Transfers	–	170,000	–	–	(170,000)	–
Transactions with equity holders, recognised directly in equity						
Final dividend approved on 24.02.2016	–	–	–	–	(662,744)	(662,744)
Total contributions from and distribution to equity holders	–	–	–	–	(662,744)	(662,744)
Balance as at 31.12.2016	4,715,814	2,004,275	14,549,487	13,779,839	10,800,251	45,849,666
Profit for the year	–	–	–	–	4,414,964	4,414,964
Other comprehensive (expenses)/ income net of tax	–	–	(1,250,801)	–	34,999	(1,215,802)
Total comprehensive/income for the year	–	–	(1,250,801)	–	4,449,963	3,199,162
Transfers	–	220,000	–	–	(220,000)	–
Transactions with equity holders, recognised directly in equity						
Forfeiture of unclaimed dividends	–	–	–	–	20,878	20,878
Final dividend approved on 20.02.2017	–	–	–	–	(1,192,940)	(1,192,940)
Total contributions from and distribution to equity holders	–	–	–	–	(1,172,062)	(1,172,062)
Balance as at 31.12.2017	4,715,814	2,224,275	13,298,686	13,779,839	13,858,152	47,876,766

	Attributable to the equity holders of the Bank								
		Statutory reserves	Other reserves						
	Stated Capital	Reserve fund	Fair value reserve	Exchange equalisation reserve	General reserve	Retained earnings	Total	Non-controlling interests	Total
	LKR 000	LKR 000	LKR 000	LKR 000	LKR 000	LKR 000	LKR 000	LKR 000	LKR 000
Group									
Balance as at 31.12.2015	4,715,814	1,834,275	11,857,655	21,910	13,779,839	11,506,206	43,715,699	252,426	43,968,125
Profit for the year	–	–	–	–	–	3,414,980	3,414,980	54,094	3,469,074
Other comprehensive income net of tax	–	–	227,799	11,518	–	143,177	382,494	176	382,670
Total comprehensive income for the year	–	–	227,799	11,518	–	3,558,157	3,797,474	54,270	3,851,744
Transfers	–	170,000	–	–	–	(170,000)	–	–	–
Transactions with equity holders, recognised directly in equity									
Change in holding through joint venture	–	–	–	–	–	(610)	(610)	–	(610)
Final dividend approved on 24.02.2016	–	–	–	–	–	(662,744)	(662,744)	–	(662,744)
Dividend distributed to non-controlling interest by subsidiaries	–	–	–	–	–	–	–	(46,796)	(46,796)
Total contributions from and distribution to equity holders	–	–	–	–	–	(663,354)	(663,354)	(46,796)	(710,150)
Balance as at 31.12.2016	4,715,814	2,004,275	12,085,454	33,428	13,779,839	14,231,009	46,849,819	259,900	47,109,719
Profit for the year	–	–	–	–	–	4,362,407	4,362,407	71,350	4,433,757
Other comprehensive income net of tax	–	–	(1,052,971)	(20,367)	–	40,681	(1,032,657)	222	(1,032,435)
Total comprehensive income for the year	–	–	(1,052,971)	(20,367)	–	4,403,088	3,329,750	71,572	3,401,322
Transfers	–	220,000	–	–	–	(220,000)	–		–
Transactions with equity holders, recognised directly in equity									
Forfeiture of unclaimed dividends	–	–	–	–	–	20,878	20,878	–	20,878
Change in holding through joint venture	–	–	–	–	–	117,478	117,478	–	117,478
Final dividend approved on 20.02.2017	–	–	–	–	–	(1,192,940)	(1,192,940)	–	(1,192,940)
Dividend distributed to non-controlling interest by subsidiaries	–	–	–	–	–	–	–	(54,600)	(54,600)
Total contributions from and distribution to equity holders	–	220,000	–	–	–	(1,054,584)	(1,054,584)	(54,600)	(1,109,184)
Balance as at 31.12.2017	4,715,814	2,224,275	11,032,483	13,061	13,779,839	17,359,513	49,124,985	276,872	49,401,857

Statement of Cash Flows

For the year ended 31 December	BANK		GROUP	
	2017 LKR 000	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Cash flows from operating activities				
Interest receipts	**25,632,064**	19,317,134	**25,630,823**	19,315,252
Interest payments	**(19,308,381)**	(13,071,125)	**(19,267,517)**	(13,039,859)
Recoveries from loans previously written off	**36,769**	24,499	**36,769**	24,499
Receipts from other operating activities	**1,338,987**	1,643,470	**1,813,361**	1,923,001
Cash payments to employees and suppliers	**(5,409,931)**	(4,657,702)	**(5,695,191)**	(4,802,292)
Value added tax and nation building tax on financial services	**(1,298,496)**	(798,410)	**(1,298,496)**	(798,410)
Other levies	**(185,529)**	(157,564)	**(185,529)**	(157,564)
Operating cash flows before changes in operating assets and liabilities	**805,483**	2,300,302	**1,034,220**	2,464,627
(Increase)/decrease in operating assets:				
Deposits held for regulatory or monetary control purposes	**(2,495,121)**	(2,508,759)	**(2,495,121)**	(2,508,757)
Funds advanced to customers	**(26,935,976)**	(33,070,446)	**(26,935,976)**	(33,070,447)
Others	**690,451**	(339,086)	**723,354**	(330,443)
Increase/(decrease) in operating liabilities:				
Deposits from customers	**50,738,651**	27,978,909	**50,599,577**	28,239,834
Negotiable certificates of deposit	**(259,665)**	32,898	**(259,665)**	32,898
Others	**206,374**	668,519	**206,374**	668,834
Net cash flows from/(used in) operating activities before income tax	**22,750,197**	(4,937,663)	**22,872,763**	(4,503,454)
Income tax paid	**(1,404,889)**	(649,287)	**(1,455,337)**	(694,286)
Net cash flows from/(used in) operating activities	**21,345,308**	(5,586,950)	**21,417,426**	(5,197,740)
Cash flows from investing activities				
Dividends received	**680,893**	688,785	**629,428**	604,526
Interest received	**6,122,521**	3,190,625	**6,171,449**	3,226,799
Government Securities – net	**(9,062,415)**	(4,102,903)	**(9,062,415)**	(4,102,903)
Proceeds from sale and redemption of securities	**2,960,619**	748,838	**2,960,619**	748,838
Purchase of securities	**(1,661,972)**	(778,566)	**(1,674,972)**	(778,566)
Investment in joint venture	**–**	(100,000)	**–**	(100,000)
Investment in additional shares of subsidiaries – (Synapsys Ltd)	**(65,000)**	–	**–**	–
Purchase of property, equipment, intangibles and investment property	**(880,905)**	(277,384)	**(992,860)**	(370,960)
Proceeds from sale of equipment and investment property	**8,944**	10,647	**16,196**	10,654
Net cash used in investing activities	**(1,897,315)**	(619,958)	**(1,952,555)**	(761,612)

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Cash flows from financing activities				
Issue of debentures	–	12,315,450	–	12,315,450
Redemption of debentures	**(5,000,000)**	(2,096,000)	**(5,000,000)**	(2,096,000)
Borrowing, medium and long-term	**11,510,776**	4,484,011	**11,510,776**	4,484,011
Other borrowings – net	**(15,718,589)**	(2,628,484)	**(15,718,589)**	(2,628,484)
Repayment of borrowing, medium and long term	**(3,943,757)**	(3,836,433)	**(3,943,757)**	(3,836,433)
Dividends paid	**(1,180,868)**	(654,832)	**(1,241,185)**	(835,442)
Net cash flows (used in)/from financing activities	**(14,332,438)**	7,583,712	**(14,392,755)**	7,403,102
Net (increase) in cash and cash equivalents	**5,115,555**	1,376,804	**5,072,116**	1,443,750
Cash and cash equivalents at the beginning of year	**5,682,051**	4,305,247	**5,760,245**	4,316,495
Cash and cash equivalents at the end of year	**10,797,606**	5,682,051	**10,832,361**	5,760,245
Reconciliation of cash and cash equivalents with items reported in the statement of financial position				
Cash and cash equivalents (Note 24)	**4,106,225**	4,330,934	**4,120,230**	4,344,260
Placements with banks (Note 26)	**6,691,381**	1,351,117	**6,712,131**	1,415,985
	10,797,606	5,682,051	**10,832,361**	5,760,245

The Statement of Cash Flows of the bank includes the results of associate, joint venture and subsidiary companies only to the extent of the cash flows between Bank and respective companies as required by Sri Lanka Accounting Standards.

Reconciliation of profit for the year to net cash flows from/(used in) operating activities.

	BANK		GROUP	
	2017 LKR 000	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Profit for the period	**4,414,964**	3,288,723	**4,433,757**	3,469,074
Add/(deduct) items not using (providing) cash:	**2,406,558**	1,321,549	**2,265,556**	1,184,244
Depreciation – Property, equipment and investment property	**259,548**	233,079	**300,142**	271,332
Amortisation – Intangible assets	**109,573**	98,262	**110,807**	98,567
Unrealised gain on Trading securities	**(91,252)**	(164,110)	**(91,252)**	(164,110)
Net loss from financial instruments at fair value through profit or loss				
– Contracts with commercial banks	**314,489**	93,944	**314,489**	93,944
– CBSL Swap	**86,277**	83,606	**86,277**	83,606
Interest rate swap fair value changes	**3,820**	2,177	**3,820**	2,177
Amortisation of deferred income on Government grant	**85,973**	(180,106)	**85,973**	(180,106)
Foreign exchange loss	**849,494**	330,157	**849,494**	330,154
Impairment for loans and other losses	**1,176,413**	937,267	**1,170,366**	916,344
Notional tax credit on Treasury Bills and Bonds	**(505,381)**	(249,914)	**(505,381)**	(249,914)
Share of profits of associate and joint venture	**–**	–	**(185,030)**	(161,151)
Provision for defined benefit plans	**117,604**	137,187	**125,851**	143,401
Deduct items reported gross under investing activities:	**(7,321,541)**	(4,123,348)	**(7,036,539)**	(4,056,979)
Dividend income	**(889,883)**	(856,306)	**(798,420)**	(772,046)
Gains on sale of financial investment	**(1,151,927)**	(156,388)	**(950,342)**	(156,388)
Gain on sale of equipment and investment property	**(11,299)**	(7,694)	**(11,299)**	(13,631)
Interest income from investments	**(5,268,432)**	(3,102,960)	**(5,276,478)**	(3,114,914)
Deduct changes in operating assets and liabilities:	**21,845,327**	(6,073,874)	**21,754,652**	(5,794,079)
(Increase)/(decrease) in account receivables	**2,922,640**	(1,645,511)	**2,468,411**	(1,660,055)
Increase in account payables	**(2,309,758)**	2,334,083	**(1,847,605)**	2,323,939
Increase/(decrease) an income tax payable	**(369,904)**	446,392	**(351,376)**	509,872
(Increase)/decrease in deferred tax	**(342,365)**	29,127	**(353,321)**	246
Increase in operating assets	**(28,740,646)**	(35,918,291)	**(28,707,743)**	(35,909,647)
Increase in operating liabilities	**50,685,360**	28,680,326	**50,546,286**	28,941,566
Net cash flow from/(used) in operating activities	**21,345,308**	(5,586,950)	**21,417,426**	(5,197,740)

Notes to the Financial Statements

1 Reporting Entity

DFCC Bank PLC ("Bank") is a limited liability public company incorporated and domiciled in Sri Lanka.

The Bank was incorporated in 1955 under DFCC Bank Act, No. 35 of 1955 as a limited liability public company and the ordinary shares of the Bank were listed in the Colombo Stock Exchange.

Consequent to the enactment of the DFCC Bank (Repeal and Consequential Provisions) Act, No. 39 of 2014, the DFCC Bank Act, No. 35 of 1955 was repealed and the Bank was incorporated under the Companies Act, No. 07 of 2007 as a public limited company listed in the Colombo Stock Exchange with the name "DFCC Bank PLC" with effect from 6 January 2015.

The Registrar General of Companies on 1 October 2015 issued the Certificate of Amalgamation in terms of Section 244 (1) (a) of the Companies Act, No. 07 of 2007 that DFCC Vardhana Bank PLC (DVB) has been amalgamated with DFCC Bank PLC in accordance with the provisions of Part VIII of the Companies Act, No. 07 of 2007 with DFCC Bank PLC surviving as the amalgamated entity.

DFCC Bank PLC (DFCC) also obtained a commercial banking license from the Monetary Board of the Central Bank of Sri Lanka in terms of the Banking Act, No. 30 of 1988, as amended, and accordingly upon the amalgamation now operates as a licensed commercial bank.

The registered office of the Bank is at 73/5, Galle Road, Colombo 3.

The Bank does not have an identifiable parent of its own. The Bank is the ultimate parent of the Group companies.

The Bank's Group comprises subsidiary companies viz, DFCC Consulting (Pvt) Limited, Lanka Industrial Estates Limited and Synapsys Limited.

A joint venture company, Acuity Partners (Pvt) Limited which is equally owned, by the Bank and Hatton National Bank PLC.

The Bank has one associate company viz, National Asset Management Limited.

Total employee population of the Bank and the Group on 31 December 2017 was 1,770and 1,869 respectively. (31 December 2016 – 1,642 and 1,760 respectively).

A summary of principal activities of DFCC Bank PLC, its subsidiary companies, associate company and joint venture company is as follows:

DFCC Bank PLC

Range of financial services such as accepting deposits, corporate credit and retail banking, personal financial services, project financing, investment banking, foreign currency operations, trade finance and dealing in Government Securities and Treasury-related products.

Subsidiaries

DFCC Consulting (Pvt) Limited

Technical, financial and other professional consultancy services in Sri Lanka and abroad.

Lanka Industrial Estates Limited

Leasing of land and buildings to industrial enterprises.

Synapsys Limited

Information technology services and information technology enabled services.

Associate

National Asset Management Limited

Fund management.

Joint Venture

Acuity Partners (Pvt) Limited

Investment banking-related financial services.

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

2 Basis of Preparation

2.1 Statement of Compliance

The consolidated financial statements of the Group and the separate financial statements of the Bank, which comprise the statement of financial position, income statement, statement of profit or loss and other comprehensive income, statement of changes in equity, statement of cash flows and notes thereto, have been prepared in accordance with Sri Lanka Accounting Standards (SLFRSs and LKASs) issued by The Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka) and in compliance with the requirements of the Companies Act, No. 07 of 2007 and the Banking Act, No. 30 of 1988 and amendments thereto.

2.2 Approval of Financial Statements by Directors

The financial statements are authorised for issue by the Board of Directors on 19 February 2018.

2.3 Consolidated and Separate Financial Statements

DFCC Bank PLC as the parent of subsidiaries under its control is required to present only the consolidated financial statements as per Sri Lanka Accounting Standard LKAS 27 – "Consolidated and Separate Financial Statements". In addition to the consolidated financial statements, separate financial statements are also presented as per the Companies Act, No. 07 of 2007 and Banking Act, No. 30 of 1988 and amendments thereto.

2.4 Basis of Measurement

The consolidated and separate financial statements of the Bank have been prepared on the historical cost basis except for the following material items in the statement of financial position:

i. Assets held-for-trading are measured at fair value.

ii. Derivative assets and derivative liabilities held for risk management are measured at fair value.

iii. Financial assets available-for-sale are measured at fair value.

iv. The liability/asset for defined benefit pension obligations is recognised as the present value of the defined benefit pension obligation less the net total of the pension assets maintained in DFCC Bank Pension Fund, a trust separate from the Bank.

v. The liability for defined benefit statutory end of service gratuity obligations is as the present value of the defined benefit gratuity obligation.

The Bank has not designated any financial instrument at fair value which is an option under LKAS 39 – "Sri Lanka Accounting Standard – Financial Instruments: Recognition and Measurement", since it does not have any embedded derivative and the Bank considers that currently, there are no significant accounting mismatches due to recognition or measurement inconsistency between financial assets and financial liabilities.

2.5 Materiality and Aggregation

Each material class of similar items is presented separately in the financial statements. Items of a dissimilar nature or function are presented separately unless they are immaterial.

2.6 Functional and Presentation Currency

The consolidated and separate financial statements of the Bank are presented in Sri Lanka Rupees (LKR) being the, functional and presentation currency, rounded to the nearest thousand and, unless otherwise stated.

2.7 Critical Accounting Estimates and Judgements

2.7.1 General

In the preparation of separate financial statements and consolidated financial statements, the Bank makes judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses.

Management discusses with the Board Audit Committee the development, selection and disclosure of critical accounting policies and their application, and assumptions made relating to major estimation uncertainties.

The use of available information and application of judgement are inherent in the formation of estimates; actual results in the future may differ from estimates upon which financial information is prepared.

Estimates and underlying assumptions are reviewed on an ongoing basis. Changes to estimates in a subsequent financial year, if any, are adjusted prospectively.

Management believes that Bank's critical accounting policies where judgement is necessarily applied are those which relate to impairment of loans and advances, financial leases and goodwill, the valuation of financial instruments, deferred tax assets and provisions for liabilities.

Further information about key assumptions concerning the future and other key sources of estimated uncertainty are set out in the notes to the financial statements.

2.7.2 Loan Losses

The assessment of loan loss as set out in Note 30.2 involves considerable judgement and estimation. Judgement is required firstly to determine whether there are indications that a loss may already have been incurred in individually significant loans and secondly to determine the recoverable amount.

2.7.3 Pension Liability

The estimation of this liability determined by an independent, qualified actuary, necessarily involves long-term assumptions on future changes to salaries, future income derived from pension assets, life expectancy of covered employees, etc. Key assumptions are disclosed in Note 48.1.3.8 on page 214.

The pension scheme is closed to new entrants recruited on or after 1 May 2004 and the basic pension and the survivor pension amount is frozen on the date of cessation of tenured employment. These risk mitigation strategies together with annual actuarial valuation and review of key assumptions tend to reduce the probability that the actual results will be significantly different from the estimate.

2.7.4 End of Service Gratuity Liability

The estimation of this liability, which is not externally funded, determined by an independent qualified actuary necessarily involves long-term assumptions on future changes to salaries, resignations prior to the normal retirement age and mortality of covered employees.

Key assumptions are disclosed in Note 48.1.3.8 on page 214.

2.7.5 Current Tax

The estimation of current tax liability includes interpretation of tax law and judgment on the allowance for losses on loans. The estimation process by the Bank includes seeking expert advice where appropriate and the payment of the current tax liability is on self-assessment basis. In the event, an additional assessment is issued, the additional income tax and deferred tax adjustment, will be in the period in which the assessment is issued, if so warranted.

2.7.6 Deferred Tax Assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that future taxable profit will be available and can be utilized against such tax losses. Judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies. Refer Note 42.2 on page 208 for details.

2.7.7 Impairment of Tangible and Intangible Assets

The assessment of impairment of tangible and intangible assets includes the estimation of the value in use of the asset computed at the present value of the best estimates of future cash flows generated by the asset adjusted for associated risks. This estimation has inherent uncertainties. Impairment losses, if any, are charged to income statement immediately.

2.8 Changes in Accounting Policies

There are no changes to the accounting policies of the Group and the Group has consistently applied the accounting policies for all periods presented in these consolidated and separate financial statements.

3 Basis of Consolidation

3.1 General

The Consolidated Financial Statements are the Financial Statements of the Group, prepared by consistent application of consolidation procedures, which include amalgamation of the Financial Statements of the parent and subsidiaries and accounting for the investments in associate company and joint venture company on the basis of reported results and net assets of the investee instead of the direct equity interest.

Thus, the Consolidated Financial Statements present financial information about the Group as a single economic entity distinguishing the equity attributable to the parent (controlling interest) and attributable to minority shareholders with non-controlling interest.

3.2 Transactions Eliminated on Consolidation

Intra-group balances and transactions, including income, expenses, and dividend are eliminated in full.

3.3 Financial Statements of Subsidiaries, Associate Company and Joint Venture Company included in the Consolidated Financial Statements

Audited financial statements are used for consolidation of companies which have a similar financial year end, as the Bank and for other a special review is performed.

Financial statements of Lanka Industrial Estates Limited included in the consolidation has financial year ending 31 March.

The financial statements of DFCC Consulting (Pvt) Limited, Acuity Partners (Pvt) Limited, Synapsys Limited and National Asset Management Limited included in the consolidation have financial years ending on 31 December.

3.4 Significant Events and Transactions during the period between Date of Financial Statements of the Subsidiaries, Associate Company and Joint Venture Company and the Date of Financial Statements of the Bank

No adjustments to the results of subsidiaries, associate company and joint venture company have been made as there were no significant events or transactions.

3.5 Financial Statements used for Computation of Goodwill or Negative Goodwill on Date of Acquisition

This is based on unaudited financial statements proximate to the date of acquisition.

3.6 Taxes on the Undistributed Earnings of Subsidiaries, Associate Company and Joint Venture Company

The distribution of the undistributed earnings of the subsidiaries, associate company and joint venture company is remote in the foreseeable future. As such, 10% withholding tax applicable on the distribution has not been treated as a tax expense in the financial statements of the Group.

4 *Scope of Consolidation*

All subsidiaries have been consolidated.

4.1 Subsidiary Companies

Subsidiaries' are investees controlled by the Group. The Group "controls" an investee if it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date when control ceases.

Acquisition method of accounting is used when subsidiaries are acquired by the Bank. Cost of acquisition is measured at the fair value of the consideration, including contingent consideration, given at the date of exchange.

Acquisition-related costs are recognised as an amount of the expense in the profit or loss in the period of which they are incurred. The acquirer's identifiable assets, liabilities and contingent liabilities are generally measured at their fair value at the date of acquisition.

Goodwill is measured as the excess of the aggregate consideration transferred, the amount of non-controlling interest and the fair value of banks previously held equity interest if any, over the net of the amount of the identifiable assets acquired and the liabilities assumed.

The amount of non-controlling interest is measured either at fair value or at the non-controlling interest's proportionate share of the acquirer's identifiable net assets.

In a business combination achieved in stages, the previously held equity interest is premeasured at the acquisition date fair value with a resulting gain or loss in the income statement.

Changes in a parent's ownership interest in a subsidiary that do not result in a loss of control are treated as transactions between equity holders and are reported in equity.

Note 33 on page 198 contains the financial information relating to subsidiaries.

4.2 Associate Company

Associate company is the enterprise over which the Bank has significant influence that is neither a subsidiary nor an interest in a joint venture. The Bank has only one associate company, National Asset Management Limited. The consolidated financial statements include the Bank's share of the total comprehensive income of the associate company, on an equity accounted basis, from the date that significant influence commences until the date that significant influence ceases.

Note 34 on page 199 contain financial information relating to associate company.

4.3 Joint Venture Company

Joint venture company is an incorporated enterprise in which the Bank owns 50% of the voting shares with a contractual arrangement with the other company, who owns the balance 50% of the voting shares, in terms of which both parties have joint control over that enterprise. The results of the joint venture company are consolidated using equity method. Note 35 on page 200 contains the financial information relating to joint venture company.

5 Principal Accounting Policies

Accounting policies are the specific principles, bases, conventions, rules and practices applied consistently by the Bank in presenting and preparing the financial statements. Changes in accounting policies are made, only if the Sri Lanka Accounting Standards require such changes or when a change results in providing more relevant information. New policies are formulated as appropriate to new products and services provided by the Bank or new obligations incurred by the Bank.

5.1 Revenue and Expense Recognition

Revenue is recognised to the extent that it is probable that the economic benefit will flow to the Group and the revenue can be reliably measured.

5.1.1 Interest Income and Expense

Details of interest income and expenses are given in Note 10 on pages 172 to 173.

5.1.2 Net Fees and Commission

Details of commission income and expenses are given in Note 11 on pages 173 to 174.

5.1.3 Net Gain from Trading

Details of net gain/loss from trading are given in Note 12 on page 174.

5.1.4 Net Gain/(Loss) from Financial Instruments at Fair Value Through Profit or Loss

Details of net gain/(loss) from Financial Instruments at Fair Value Through Profit or Loss are given in Note 13 on page 174.

5.1.5 Net Gain/(Loss) from Financial Investments

Details of net gain/(loss) from financial instruments are given in Note 14 on page 175.

5.1.6 Foreign Exchange Gain/(Loss)

Items included in the financial statements of the Bank are measured in Sri Lankan Rupees denoted as LKR which is the currency of the primary economic environment in which the Bank operates ("the functional currency") as well as the presentation currency.

Transactions in foreign currencies are recorded in the functional currency at the average exchange rate on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the average exchange rate ruling at the reporting date (viz. date of the statement of financial position) and consequently recognised in the "other operating (loss)/income" in the income statement of the Bank. The average exchange rate used is the middle rates quoted by commercial banks for purchase or sale of the relevant foreign currency.

The Bank does not have any non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency.

Foreign exchange income recognised in the income statement is presented as follows, based on the underlying classification:

i. Foreign exchange gain/(loss) which is part of a trading activity comprising profit or loss from the sale and purchase of foreign currencies for spot exchange is included as net gain from trading (Note 12).

ii. Foreign exchange income or loss on derivatives held-for-risk management purposes and mandatory measured at fair value through profit or loss is recognised as net gain/loss from financial instruments at fair value through profit or loss (Note 13).

The Bank does not have any foreign operation that is a subsidiary, associate, joint venture or a branch and therefore, there is no exchange differences recognised in other comprehensive income.

5.1.7 Other Expenses

All other expenses are recognised on an accrual basis.

5.2 Other Taxes

5.2.1 Withholding Tax on Dividend Distributed by Subsidiaries, Associate Company and Join Venture Company.

Dividend distributed out of the taxable profit of the subsidiaries, associate company and joint venture company suffers a 10% deduction at source and is not available for set-off against the tax liability of the Bank. Thus the withholding tax deducted at source, is added to the tax expense of the subsidiary companies, the associate company and joint venture company in the Group's financial statements as a consolidation adjustment.

5.2.2 Withholding Tax on Dividends Distributed by the Bank.

Withholding tax that arises from the distribution of dividends by the Bank is recognised at the time the liability to pay the related dividend is recognised .

5.2.3 Economic Services Charge (ESC)

As per provisions of the Economic Services Charge (ESC) Act, No. 13 of 2006 and subsequent amendments thereto, ESC is payable on aggregate turnover of the Bank at 0.5% and is deductible from income tax payable.

5.2.4 Crop Insurance Levy (CIL)

As per the provisions of the Section 14 of the Finance Act, No. 12 of 2013, the CIL was introduced with effect from 01st of April 2013 and is payable to the National Insurance Trust Fund. Currently the CIL is payable at 1% of the profit after tax.

5.3 Financial Assets

5.3.1 Recognition and Measurement

The financial asset is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction cost that are directly attributable to its acquisition.

Loans and advances are initially recognised on the date at which they are originated at fair value which is usually the loan amount granted and subsequent measurement is at amortised cost.

The amortised cost of a financial asset is the amount at which the financial asset is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

All other financial assets are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

5.3.2 Classification

At the inception, a financial asset is classified and measured at fair value and classified as follows:

- **Loans and receivables** – at amortised cost.
- **Held to maturity** – non-derivative financial assets with fixed or determinable payments and fixed maturity (for example, bonds, debentures and debt instruments listed in the Colombo Stock Exchange) that the Bank has the positive intent and ability to hold to maturity are measured at amortised cost.
- **Fair value through profit or loss** – financial assets held-for-trade measured at fair value with changes in fair value recognised in the income statement.
  - **Designated at fair value** – this is an option to deal with accounting mismatches and currently the Bank has not exercised this option.
  - **Derivative assets** – are mandatorily measured at fair value with fair value changes recognised in the income statement.
- **Available for sale** – this is measured at fair value and is the residual classification with fair value changes recognised in other comprehensive income.

5.3.3 Reclassification

- Non-derivative financial assets (other than those designated at fair value through profit or loss upon initial recognition) may be reclassified out of the fair value through profit or loss category, in the following circumstances:
- Financial assets that would have met the definition of loans and receivables at initial recognition (if the financial asset had not been required to be classified as held for trading) may be reclassified out of the fair value through profit or loss category if there is the intention and ability to hold the financial asset for the foreseeable future or until maturity; and
- Financial assets except financial assets that would have met the definition of loans and receivables at initial recognition may be reclassified out of the fair value through profit or loss category and into another category in rare circumstances.

5.3.4 *Derecognition of Financial Assets*

Financial assets are derecognised when the contractual right to receive cash flows from the asset has expired; or when Bank has transferred its contractual right to receive the cash flows of the financial assets, and either –

- Substantially all the risks and rewards of ownership have been transferred;
  or
- Bank has neither retained nor transferred substantially all the risks and rewards, but has not retained control of the financial asset.

5.3.5 *Fair Value Measurement*

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

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

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

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e., the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price.

Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

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

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

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

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

5.3.6 *Identification and Measurement of Impairment*

At each reporting date, the Bank assesses whether there is an objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s) that can be estimated reliably.

5.3.6.1 *Loans and Advances and Held-to-Maturity Investment Securities*

Objective evidence that loans and advances and held-to-maturity investment securities (e.g., debt instruments quoted in the Colombo Stock Exchange, Treasury Bills and Bonds) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the Group or economic conditions that correlate with defaults in the Group.

The Bank considers evidence of impairment for loans and advances and held-to-maturity investment securities at both a specific and collective level. Details of the individual and collective assessment of impairments are given in Note 16 on pages 176 and 177.

5.3.6.2 Available-for-Sale Financial Assets

At each date of statement of financial position an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset. Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the financial asset (a "loss event") and that loss event (or events) have an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

If the available-for-sale financial asset is impaired, the difference between the financial asset's acquisition cost (net of any principal repayments and amortisation) and the current fair value, less any previous impairment loss recognised in the income statement, is removed from other comprehensive income and recognised in the income statement.

5.3.6.3 Available-for-Sale Debt Securities

When assessing available-for-sale debt securities for objective evidence of impairment at the reporting date. Bank considers all available evidence, including observable data or information about events specifically relating to the securities which may result in a shortfall in recovery of future cash flows. These events may include a significant financial difficulty of the issuer, a breach of contract such as a default, bankruptcy or other financial recognition, or the disappearance of an active market for the debt security.

These types of specific events and other factors such as information about the issuers' liquidity, business and financial risk exposures, levels of and trends in default for similar financial assets, national and local economic trends and conditions, and the fair value of collateral and guarantees may be considered individually, or in combination, to determine if there is objective evidence of impairment of a debt security.

5.3.6.4 Available-for-Sale Equity Securities

Objective evidence of impairment for available-for-sale equity securities may include specific information about the issuer and information about significant changes in technology, markets, economics or the law that provide evidence that the cost of the equity securities may not be recovered.

A significant or prolonged decline in the fair value of the asset below its cost is also objective evidence of impairment. In assessing whether it is significant, the decline in fair value is evaluated against the original cost of the asset at initial recognition. In assessing whether it is prolonged, the decline is evaluated against the period in which the fair value of the asset has been below its original cost at initial recognition.

Once an impairment loss has been recognised on an available-for-sale financial asset, the subsequent accounting treatment for changes in the fair value of that asset differs depending on the nature of the available-for-sale financial asset concerned:

- For an available-for-sale debt security, a subsequent decline in the fair value of the instrument is recognised in the income statement when there is further objective evidence of impairment as a result of further decreases in the estimated future cash flows of the financial asset. Where there is no further objective evidence of impairment, a decline in the fair value of the financial asset is recognised in other comprehensive income. If the fair value of a debt security increases in a subsequent period, and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement. If there is no longer objective evidence that the debt security is impaired, the impairment loss is also reversed through the income statement.
- For an available-for-sale equity security, all subsequent increases in the fair value of the instrument are treated as a revaluation and are recognised in other comprehensive income. Impairment losses on the equity security are not reversed through the income statement. Subsequent decreases in the fair value of the available-for-sale equity security are in the income statement, to the extent that further cumulative impairment losses have been incurred in relation to the acquisition cost of the equity security.

5.3.6.5 Impairment of Intangible Assets – Computer Application Software and Goodwill on Consolidation

The Bank reviews on the date of the statement of financial position, whether the carrying amount is lower than the recoverable amount. In such event, the carrying amount is reduced to the recoverable amount and the reduction being an impairment loss is immediately recognised in the income statement. The recoverable amount is the value in use.

5.3.7 Offsetting

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to offset the amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted under SLAS or for gains and losses arising from a group of similar transactions.

5.3.8 Fiduciary Assets

Assets held in a fiduciary capacity are not reported in these financial statements as they do not belong to the Bank.

5.4 Financial Liabilities

5.4.1 Recognition and Initial Measurement

Deposits, borrowing from foreign multilateral, bilateral sources and domestic sources, debt securities issued and subordinated liabilities are initially recognised on the date at which they are originated. A financial liability is measured initially at fair value plus, transaction costs that are directly attributable to its acquisition or issue.

Subsequent measurement of financial liability is at fair value or amortised cost. The amortised cost of a financial liability is the amount at which the financial liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount and the maturity amount.

5.4.2 Derecognition of Financial Liabilities

Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expired.

5.4.3 Due to Banks, Customers, Debt Securities Issued and Other Borrowing

Financial liabilities are recognised when Group enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at fair value, which is normally the consideration received, net of directly attributable transaction costs incurred. Subsequent measurement of financial liabilities is at amortised cost, using the effective interest method to amortise the difference between proceeds received, net of directly attributable transaction costs incurred, and the redemption amount over the expected life of the instrument.

5.4.4 Provisions

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

5.4.5 Sale and Repurchase Agreements

When securities are sold subject to a commitment to repurchase them at a predetermined price ("repos"), they remain on the statement of financial position and a liability is recorded in respect of the consideration received.

Securities purchased under commitments to sell ("reverse repos") are not recognised on the statement of financial position and the consideration paid is recorded in "loans and advances to banks", "loans and advances to customers" as appropriate. The difference between the sale and repurchase price is treated as interest and recognised over the life of the agreement for loans and advances to banks and customers.

5.5 Stated Capital

Shares are classified as equity when there is no contractual obligation to transfer cash or other financial assets.

6 Cash Flow

The cash flow has been prepared by using the "Direct Method". Cash and cash equivalents include cash balances, time deposits and Treasury Bills of three months maturity at the time of issue. For the purpose of cash flow statement, cash and cash equivalents are presented net of bank overdrafts.

7 Directors' Responsibility

The Directors acknowledge the responsibility for true and fair presentation of the financial statements in accordance with Sri Lanka Accounting Standards.

8 New SLFRS Issued and Not Yet Effective

8.1 SLFRS Applicable for Financial Periods beginning on or after 1 January 2018

8.1.1 SLFRS 9 – *"Financial Instruments"*

SLFRS 9, issued in 2014, replaces the existing guidance in LKAS 39 – "Financial Instruments: Recognition and Measurement" is effective for annual reporting periods beginning on or after 1 January 2018. The key aspects of SLFRS 9 are:

1. Classification – Financial assets

   SLFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

   SLFRS 9 includes three principal classification categories for financial assets – i.e. measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). It eliminates the existing LKAS 39 categories of held-to-maturity, loans and receivables and available for sale.

2. Impairment – Financial assets, loan commitment and financial guarantee contracts

   SLFRS 9 replaces the 'Incurred Loss Model in LKAS 39 with forward looking "Expected Loss Model '(ECL). This will require considerable judgement over how changes in economic factors affect ECL, which will be determined in a probability weighted basis.

   SLFRS 9 requires loan loss to be recognised at an amount equal to either 12 month ECL or life time ECL. Lifetime ECLs are the ECLs that result from possible default events over the expected life of a financial instrument, whereas 12 months ECLs are the portion of the ECLs that results from default events that are possible within 12 months after the reporting date.

3. Inputs into measurement of ECLs

   The key inputs into measurement of ECLs are likely to be the term structures of the following variables which will be derived from internally developed statistical models and other historical data that leverage regulatory models. They will be adjusted to reflect forward looking information.

- Probability of Default (PD) are estimates at a certain date which will be calculated based on statistical models and assessed using rating tools tailored to the various categories of counterparties and exposures
- Loss Given Default (LGD) is the magnitude to the likely loss if there is default. The Bank estimates LGD parameters based on history of recovery rates of claims against defaulted counter parties
- Exposure at Default (EAD) represents the expected exposure in the event of a default. The Bank will derive the EAD from the current exposure to the counter party and potential chances to the current amount allowed under the contract.

The most significant impact on the Bank's Financial Statements from the implementation of SLFRS 9 is expected to result from the new impairment requirements. Impairment losses will increase and become more volatile for financial instruments within the scope of SLFRS 9.

The Bank has employed statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposure and how these are expected to change as a result of the passage of time. This analysis include the identification and calibration of relationship between changes in default rates and changes in key macroeconomic factors as well as analysis of the impact of certain other factors on the risk of default.

The Bank has estimated LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset.

EAD for lending commitments and financial guarantees, include the amount drawn, as well as potential future amounts that may be drawn or repaid under the contract, which has been estimated based on historical observations and forward looking forecasts.

Under SLFRS 9, the Bank has incorporated forward looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL.

The Bank has completed the initial high level assessment of the potential impact on its Financial Statements for the year ended 31 December 2016, resulting from the application of SLFRS 9 with the assistance of an external consultant.

Based on the preliminary assessments undertaken to date which is yet to be audited, the total estimated additional loan loss provision on the financial statements for the year ended 31 December 2016 on adoption of SLFRS 9 is expected to be in the range of 35% to 40%. It will also have an impact on capital adequacy ratio by 99 to 115 basis points on Tier 1 due to the reduction in the retained earnings.

The above assessment which is yet to be audited is preliminary because not all transition work has been finalised. The actual impact of adopting SLFRS 9 on 1 January 2018 may change because:

- SLFRS 9 will require the Bank to revise accounting process and internal controls and these changes are not yet complete;
- The Bank is refining and finalising its models for ECL calculations; and
- The new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Bank finalises its first Financial Statements for the year 31 December 2018 that include the date of initial application.

The Bank is in the process of assessing the additional loan loss provision impact on the Financial Statements for the year ended 31 December 2017, resulting from the application of SLFRS 9.

The Group does not expect significant impact on the Consolidated Financial Statements resulting from the application of SLFRS 9 on the other group entities.

8.1.2 SLFRS 15 – "Revenue from Contracts with Customers"

SLFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised . New qualitative and quantitative disclosure requirements aim to enable financial statements users to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

Entities will apply five step model to determine when to recognise revenue and at what amount. The model specified that revenue is recognised when or as an entity transfers control of goods and services to a customer at the amount to which the entity expects to be entitled. Depending on whether certain criteria are met, revenue is recognised .

It replaces existing revenue recognition guidance, including LKAS 18 – "Revenue" and LKAS 11 – "Construction Contracts" and IFRIC 13 – "Customer Loyalty Programmes". SLFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

The Group/Bank does not expect significant impact on its financial statements resulting from the application of SLFRS 15.

8.1.3 SLFRS 16 – "Leases"

SLFRS 16 eliminates the current dual accounting model for lessees which distinguishes between On-Balance Sheet finance leases and Off-Balance Sheet operating leases.

Instead, there will be a single On-Balance Sheet accounting model that is similar to current finance lease accounting.

SLFRS 16 is effective for annual reporting periods beginning on or after 01 January 2019. The Group/Bank is assessing the potential impact on its financial statements resulting from the application of SLFRS 16.

9 Income

Accounting Policy →

Revenue is recognised to the extent that it is probable that the economic benefit will flow to the Group and the revenue can be reliably measured.

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Interest income (Note 10)	**32,986,590**	24,194,158	**32,994,636**	24,206,112
Fee and commission income (Note 11)	**1,591,336**	1,309,049	**1,591,943**	1,309,049
Net gain from trading (Note 12)	**361,647**	340,456	**361,647**	340,456
Net loss from financial instruments at fair value through profit or loss (Note 13)	**(404,586)**	(179,727)	**(404,586)**	(179,727)
Net gain from financial investments (Note 14)	**2,238,166**	1,165,389	**1,945,118**	1,081,129
Other operating (loss)/income – net (Note 15)	**(831,541)**	(75,430)	**(501,667)**	223,064
	35,941,612	26,753,895	**35,987,091**	26,980,083

10 Net Interest Income

Accounting Policy →

Interest income and expense for all interest-bearing financial instruments are recognised in "Interest Income" and "Interest Expense" in the income statement, using the effective interest rate of the financial assets or financial liabilities to which they relate.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments earned or paid on a financial asset or financial liability through its expected life (or, where appropriate, a shorter period) to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, bank estimates future cash flows considering all contractual terms of the financial instruments but not future credit losses.

The calculation of the effective interest includes all transaction cost, premiums or discounts and fees paid or received by the Bank that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income includes income from finance leases, dividend from preference shares and notional tax credit on interest income from Treasury Bills and Bonds.

Finance lease income is recognised on a pattern reflecting a constant periodic rate of return on the Bank's net investment in the finance lease.

For the year ended 31 December	BANK		GROUP	
	2017 LKR 000	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Interest income				
Placements with banks	**123,369**	203,105	**131,415**	215,059
Loans to and receivables from banks	**928,176**	531,828	**928,176**	531,828
Loans to and receivables from other customers	**26,789,982**	20,559,370	**26,789,982**	20,559,370
Other financial assets held for trading	**41,523**	154,544	**41,523**	154,544
Financial investments – available for sale	**2,433,596**	1,587,178	**2,433,596**	1,587,178
Financial investments – held to maturity	**2,669,944**	1,158,133	**2,669,944**	1,158,133
Total interest income	**32,986,590**	24,194,158	**32,994,636**	24,206,112
Interest expenses				
Due to banks	**979,281**	1,293,423	**979,281**	1,293,423
Due to other customers	**15,293,031**	9,552,556	**15,246,422**	9,522,440
Other borrowing	**1,645,138**	1,366,328	**1,645,138**	1,366,328
Debt securities issued	**3,726,532**	3,080,715	**3,726,532**	3,080,715
Total interest expenses	**21,643,982**	15,293,022	**21,597,373**	15,262,906
Net interest income	**11,342,608**	8,901,136	**11,397,263**	8,943,206
Interest income on Sri Lanka Government Securities	**5,032,032**	2,485,194	**5,032,032**	2,485,194

This income includes notional tax credit of 10% imputed for the withholding tax deducted/paid at source.

11 Net Fee and Commission Income

Accounting Policy →

Fee and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, the related loan commitment fees are recognised on a straight-line basis over the commitment period.

Fees for guarantees and trade related commissions are recognised on a straight line basis over the period of the contract. Other fees and commission expense relate mainly to transaction and service fees, which are expensed, as the services are received.

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Fee and commission income	**1,591,336**	1,309,049	**1,591,943**	1,309,049
Fee and commission expenses	–	–	–	–
Net fee and commission income	**1,591,336**	1,309,049	**1,591,943**	1,309,049
Comprising:				
Loans and advances	**553,094**	403,589	**553,094**	403,589
Credit cards	**4,932**	4,820	**4,932**	4,820
Trade and remittances	**429,528**	390,020	**429,528**	390,020
Customer accounts	**342,984**	281,056	**342,984**	281,056
Guarantees	**206,798**	161,805	**206,798**	161,805
Management and consulting and other fees	**54,000**	67,759	**54,607**	67,759
Net fee and commission income	**1,591,336**	1,309,049	**1,591,943**	1,309,049

12 Net Gain from Trading

This comprises all gains less losses from changes in fair value of financial assets held for trading (both realised and unrealised) together with related dividend and foreign exchange differences.

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Foreign exchange from banks	**270,395**	176,346	**270,395**	176,346
Fixed income	**67,536**	164,110	**67,536**	164,110
Equities	**23,716**	–	**23,716**	–
	361,647	340,456	**361,647**	340,456

13 Net loss from financial instruments at fair value through profit or loss

Accounting Policy →

Bank has not chosen the option to designate financial instruments at fair value through profit or loss as a compensatory mechanism for accounting mismatches that would otherwise arise from measuring assets or liabilities or recognising gains or losses on them on different bases.

The Bank has non-trading derivatives held for risk management purposes (e.g., forward foreign exchange purchase or sale contracts) that do not form part of qualifying hedge relationship, that are mandatorily fair valued through profit or loss. In respect of such financial instruments, all realised and unrealised fair value changes and foreign exchange differences are included.

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Forward exchange fair value changes				
Contracts with commercial banks	**(314,489)**	(93,944)	**(314,489)**	(93,944)
Contract with CBSL (Note 41.1)	**(86,277)**	(83,606)	**(86,277)**	(83,606)
Interest rate swap fair value changes	**(3,820)**	(2,177)	**(3,820)**	(2,177)
	(404,586)	(179,727)	**(404,586)**	(179,727)

14 Net Gain from Financial Investments

Accounting Policy →

Dividend income is recognised when the right to receive payment is established. Dividend income are presented in net gains/(loss) from trading and net gains/(loss) from financial investment, based on underlying classification of the equity investment.

Net gain/loss from financial investments includes realised gain or loss on sale of available-for-sale securities (e.g., Treasury Bills and Bonds, ordinary shares – both listed in the Colombo Stock Exchange and unlisted) and dividend income from ordinary shares classified as available for sale. Where the dividend clearly represents a recovery of part of the cost of the investment, it is presented in other comprehensive income.

	BANK		GROUP	
For the year ended 31 December	**2017 LKR 000**	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Assets available for sale				
Gain on sale of equity securities	**1,150,368**	152,186	**948,783**	152,186
Gain on sale of Government Securities	**1,559**	4,202	**1,559**	4,202
Dividend income	**798,420**	772,046	**798,420**	772,046
Dividend income from subsidiaries, joint venture and associate	**91,463**	84,260	**–**	–
Net gain from repurchase transactions	**196,356**	152,695	**196,356**	152,695
	2,238,166	1,165,389	**1,945,118**	1,081,129

15 Other operating income/(loss) – net

Accounting Policy →

Rental income and expenses are accounted on a straight-line basis over the entire period of the tenancy incorporating predetermined rent escalation during the period of the tenancy.

	BANK		GROUP	
For the year ended 31 December	**2017 LKR 000**	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Premises rental income	**39,383**	37,815	**262,021**	228,951
Gain on sale of property, plant and equipment	**11,299**	7,694	**11,299**	13,631
Foreign exchange loss	**(849,494)**	(330,157)	**(849,494)**	(330,154)
Recovery of loans written off	**36,769**	24,499	**36,769**	24,499
Amortisation of deferred income on Government Grant – CBSL Swap (Note 41.2)	**(85,973)**	180,106	**(85,973)**	180,106
Others	**16,475**	4,613	**123,711**	106,031
	(831,541)	(75,430)	**(501,667)**	223,064

16 Impairment for Loans and Other Losses

Accounting Policy →

Individually Assessed Loans and Advances and Held-to-Maturity Debt Instruments

These are exposures, where evidence of impairment exists and that are individually significant meriting individual assessment for objective evidence of impairment and computation of impairment allowance. The factors considered in determining that the exposures are individually significant include

- *the size of the loan; and*
- *the number of loans in the portfolio.*

For all loans and held-to-maturity debt instruments that are considered individually significant, Bank assesses on a case by case basis, whether there is any objective evidence of impairment. The criteria used by the Bank to determine that there is such objective evident include

- *contractual payments for either principal or interest being past due for a prolonged period;*
- *the probability that the borrower will enter bankruptcy or other financial realisation;*
- *a concession granted to the borrower for economic or legal reasons relating to the borrower's financial difficulty that results in forgiveness or postponement of principal, interest or fees, where the concession is not insignificant; and*
- *there has been deterioration in the financial condition or outlook of the borrower such that its ability to repay is considered doubtful.*

For those loans and held-to-maturity investment securities where objective evidence of impairment exists, impairment losses are determined considering the following factors:

- *Bank'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 likely dividend available on liquidation or bankruptcy;*
- *the extent of other creditors' commitments ranking ahead of or pari passu with, the Bank and*
- *the likelihood of other creditors continuity to support the Company;*
- *the realisable value of security (or other credit mitigants) and likelihood of successful repossession or enforcement of security;*
- *the likely deduction of any costs involved in recovery of amounts outstanding.*

Impairment allowance on loans and advances and held-to-maturity investment securities measured at amortised cost are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

Collective Assessment, this includes:

All loans and advances of smaller value where there is no evidence of impairment and those individually assessed for which no evidence of impairment has been specifically identified on an individual basis.

- *Import loans*
- *Export loans*
- *Corporate term loans*
- *Overdraft*
- *Personal loans*
- *Finance leases*
- *Project Loans*
- *Credit Cards*

These loans and advances are grouped together according to their credit risk characteristics for the purpose of calculating an estimated collective impairment.

In assessing collective impairment, the Bank uses statistical modelling of historical trends of the default rates, the timing of recoveries and the amount of loss incurred, adjusted for experience adjustment by the management, where current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

Default rates, loss rates and the expected timing of future recoveries will be regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Individually assessed loans for which, no evidence of impairment 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 impairment. This reflects impairment losses that Bank has incurred as a result of events occurring before the reporting date which the Bank is not able to identify on an individual 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 held-to-maturity investment securities within the Group, these are removed from the Group and assessed on an individual basis for impairment. The collective impairment allowance is based on historical loss experience adjusted by Management's experienced judgement.

Impairment allowance on loans and advances and held-to-maturity investment securities measured at mortised cost are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

Reversals of Impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the loan impairment allowance accordingly. The write back is recognised in the income statement.

Renegotiated Loans

Loans subject to collective impairment assessment whose terms have been renegotiated are no longer considered past due, but are treated as up-to-date loans for measurement purposes once a minimum number of payments required have been received.

Loans subject to individual impairment assessment, whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired. The carrying amounts of loans that have been classified as renegotiated retain this classification until maturity or derecognition.

Write-off of Loans and Advances

Loans (and the related impairment allowance) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

Asset-Backed Securities

These are included in loans and advances. When assessing for objective evidence of impairment, Bank considers the performance of underlying collateral.

	BANK		GROUP	
For the year ended 31 December	**2017 LKR 000**	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Loans to and receivables from other customers				
Specific allowance for impairment (Note 30.2.1)	**724,402**	792,389	**724,402**	792,389
Collective allowance for impairment (Note 30.2.2)	**405,973**	81,772	**405,973**	81,772
Impairment charge/(recoveries) – other debts	**17,748**	5,371	**21,597**	5,371
Impairment charge – investment in other equity securities	**12,915**	33,929	**12,915**	33,929
Impairment charge – investment in subsidiaries (Note 33.1)	**9,896**	20,923	–	–
Write-offs – loans to and receivables from other customers	**5,479**	2,883	**5,479**	2,883
	1,176,413	937,267	**1,170,366**	916,344

17 Personnel Expenses

Accounting Policy →

Employee Benefits

Defined Benefit Plans (DBPs)

A Defined Benefit Plan is a post-employment benefit plan other than a Defined Contribution Plan as defined in the Sri Lanka Accounting Standard – LKAS 19 on "Employee Benefits".

Pension Liability Arising from Defined Benefit Obligations

Description of the Plan and Employee Groups Covered

The Bank established a trust fund in May 1989, for payment of pension which operates the pension scheme approved by the Commissioner General of Inland Revenue. The fund of the scheme is managed by trustees appointed by the Bank and is separate from the Bank. The scheme provides for payment of pension to retirees, spouse and minor children of deceased retirees based on pre-retirement salary. All members of the permanent staff who joined prior to 1 May 2004 are covered by this funded pension scheme subject to fulfilment of eligibility conditions prescribed by the Bank.

The scheme was amended on 31 August 1998 and the amended plan will apply to all members of the permanent staff who joined the Bank on or after this date and prior to 1 May 2004. The amendment reduced the scope of the benefit in the interest of long-term sustainability of the pension plan as advised by the independent actuary.

The defined benefit pension plan does not permit any post-retirement increases in pension nor any other benefit (e.g. medical expenses reimbursement).

Funding Arrangement

The Bank's contributions to the trust fund are made annually based on the recommendation of an independent actuary. The employees make no contributions to qualify for the basic pension, which is therefore a non-contributory benefit to the employees.

Eligible employees who desire to provide for the payment of pension to spouse and minor children, who survive them are however, required to contribute monthly, an amount based on a percentage of gross emoluments, excluding bonus, if they joined the Bank on or after 31 August 1998 and prior to 1 May 2004.

Recognition of Actuarial Gains and Losses

The net actuarial gains or losses arising in a financial year is due to increases or decreases in either the present value of the promised pension benefit obligation or the fair value of pension assets.

The causes for such gains or losses include changes in the discount rate, differences between the actual return and the expected return on pension assets and changes in the estimates of actual employee turnover, mortality rates and increases in salary.

The Bank recognises the total actuarial gains and losses that arise in calculating the Bank's obligation in respect of the plan in other comprehensive income and the expense under personnel expenses in the income statement during the period in which it occurs.

Recognition of Past Service Cost

Past service cost arises when a defined benefit plan is introduced for the first time or subsequent changes are made to the benefits payable under an existing defined benefit plan. Bank will recognise past service cost as an expense on a straight-line basis over the average period until the benefits become vested. To the extent the benefits are already vested following the introduction of or changes to a defined benefit plan, the Bank will recognise past service cost immediately.

Provision for End of Service Gratuity Liability under a Defined Benefit Plan

Description of the Plan and Employee Groups Covered

The Bank provides for the gratuity payable under the Payment of Gratuity Act, No. 12 of 1983 as amended for all employees who do not qualify under the pension scheme. Therefore, this applies to employees recruited to the permanent cadre on or after 1 May 2004 on tenured or fixed term contract employment in the Bank. The subsidiary companies, which do not have a non-contributory pension scheme provide for the gratuity payable under the Payment of Gratuity Act, No. 12 of 1983 for all employees. The promised benefit is half a month pre-termination salary for each completed year of service, provided a minimum qualifying period of 5 years is served prior to termination of employment.

The Bank however, recognises the liability by way of a provision for all employees in tenured employment from the date they joined the permanent cadre, while fixed term employees liability is recognised only if the fixed term contract of service provides for unbroken service of 5 years or more either singly or together with consecutive contracts.

Funding Arrangement

The Bank and the subsidiaries adopt a pay-as-you-go method whereby the employer makes a lump sum payment only on termination of employment by resignation, retirement at the age of 55 years or death while in service.

Recognition of Actuarial Gains and Losses

The Bank recognises the total actuarial gains and losses in the other comprehensive income during the period in which it occurs.

Recognition of Past Service Cost

Since end of service gratuity defined benefit is a statutory benefit, the recognition of past service cost will arise only if the Payment of Gratuity Act, No. 12 of 1983 is amended in future to increase the promised benefit on termination of employment. In such event, the Bank will adopt the accounting policy currently used for defined benefit pension plan.

Defined Contribution Plans

This provides for a lump sum payment on termination of employment by resignation, retirement at the age of 55 years or death while in service.

Lump sum payment is by an outside agency to which contributions are made.

All employees of the Bank are members of the Mercantile Service Provident Society and the Employees' Trust Fund to which the Bank contributes 15% and 3% respectively of such employee's consolidated salary.

Contributions to defined contribution plans are recognised as an expense in the income statement as incurred.

For the year ended 31 December	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Salaries and other benefits	**2,770,383**	2,429,063	**2,880,514**	2,574,073
Provision for staff retirement benefits (Note 17.1)	**396,126**	380,679	**422,279**	405,996
	3,166,509	2,809,742	**3,302,793**	2,980,069

17.1 Provision for Staff Retirement Benefits

17.1.1 Amount Recognised as Expense

17.1.1.1 Funded Pension Liability

	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Current service cost	**60,496**	71,746	**60,496**	71,746
Interest on obligation	**228,094**	206,681	**228,094**	206,681
Expected return on pension assets	**(233,917)**	(193,785)	**(233,917)**	(193,785)
	54,673	84,642	**54,673**	84,642

17.1.1.2 Unfunded Pension Liability

	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Interest on obligation	**5,794**	5,688	**5,794**	5,688
	5,794	5,688	**5,794**	5,688

17.1.1.3 Unfunded End of Service Gratuity Liability

	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Current service cost	**35,041**	29,417	**41,507**	33,853
Interest on obligation	**22,096**	17,440	**23,877**	19,218
	57,137	46,857	**65,384**	53,071
Total defined benefit plans	**117,604**	137,187	**125,851**	143,401

17.1.1.4 Defined Contribution Plan

	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Employer's contribution to employees' provident fund	**232,102**	202,910	**245,952**	218,284
Employer's contribution to employees' trust fund	**46,420**	40,582	**50,476**	44,311
Total defined contribution plans	**278,522**	243,492	**296,428**	262,595
Total expense recognised in the income statement	**396,126**	380,679	**422,279**	405,996

18 Other Expenses

For the period ended	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
Directors' remuneration	**17,241**	18,582	**18,117**	19,472
Auditors' remuneration				
Audit fees and expenses	**5,207**	3,900	**5,975**	4,623
Audit related fees and expenses	**1,706**	1,265	**1,889**	1,316
Fees for non-audit services	**4,750**	1,150	**4,750**	1,150
Depreciation – investment property	–	–	**13,718**	13,800
– property, plant and equipment	**259,548**	233,079	**286,424**	257,532
Amortisation – intangible assets	**109,573**	98,262	**110,807**	98,567
Expenses on litigation	**4,728**	2,767	**4,728**	2,767
Premises, equipment and establishment expenses	**1,285,640**	1,049,987	**1,309,156**	1,048,935
Other overhead expenses	**1,015,253**	905,232	**995,866**	873,475
	2,703,646	2,314,224	**2,751,430**	2,321,637

Directors' remuneration include fees paid to Non-Executive Directors. Remuneration paid to Executive Directors are included under salaries and other benefits in Note 17.

19 Value Added Tax and Nation Building Tax on Financial Services

Value Added Tax on Financial Services (VAT)

Accounting Policy →

VAT on financial services is calculated in accordance with Value Added Tax Act, No. 14 of 2002 and subsequent amendments thereto.

The value base for computation of VAT is the operating profit before value added tax and nation building tax on financial services adjusted for emoluments of employees and depreciation computed as per prescribed rates.

Nation Building Tax on Financial Services (NBT)

NBT on financial services is calculated in accordance with Nation Building Tax Act, No. 09 of 2009 and subsequent amendments thereto. NBT is chargeable on the same base used for calculation of VAT on financial services.

For the period ended	BANK 2017 LKR 000	BANK 2016 LKR 000	GROUP 2017 LKR 000	GROUP 2016 LKR 000
19.1 Value Added Tax on Financial Services				
Financial services VAT – Current year	**1,286,661**	854,680	**1,286,661**	854,680
– (Over)/under provision in respect of previous year	–	2,495	–	2,495
	1,286,661	857,175	**1,286,661**	857,175

For the period ended	BANK		GROUP	
	2017 LKR 000	2016 LKR 000	**2017 LKR 000**	2016 LKR 000

19.2 Nation Building Tax on Financial Services

Nation building tax on				
Financial services – Current year	**171,554**	137,105	**171,554**	137,105
– Over provision in respect of previous year	**534**	(8,170)	**534**	(8,170)
	172,088	128,935	**172,088**	128,935
	1,458,749	986,110	**1,458,749**	986,110

20 Income Tax Expense

Accounting Policy →

Income Tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in the income statement except to the extent that they relate to items recognized directly in equity and other comprehensive income.

Current Taxation

Current tax is the amount of income tax payable on the taxable profit for the financial year calculated using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Taxable profit is determined in accordance with the provisions of Inland Revenue Act, No 10 of 2006 as amended.

Deferred Taxation

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax is calculated using the tax rates expected to apply in the periods in which the assets will be realised or the liabilities settled. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets.

Withholding Tax on Dividend Distributed by Subsidiaries, Associate Company and Joint Venture Company

Dividend distributed out of the taxable profit of the subsidiaries, associate company and joint venture company suffers a 10% deduction at source and is not available for set off against the tax liability of the Bank. Thus the withholding tax deducted at source is added to the tax expense of the subsidiary companies, the associate company and joint venture company in the Group financial statements as a consolidation adjustment.

For the year ended 31 December	BANK		GROUP	
	2017 LKR 000	2016 LKR 000	**2017 LKR 000**	2016 LKR 000

20.1 Composition

Current tax	**1,321,584**	1,027,194	**1,388,734**	1,084,646
(Over)/Under provision in previous years	**(20,655)**	57,912	**(20,627)**	57,827
Deferred tax – Origination and reversal of temporary differences (Note 42)	**76,420**	39,701	**89,546**	62,621
	1,377,349	1,124,807	**1,457,653**	1,205,094

20.1.1 Reconciliation of Effective Tax Rate with Income Tax Rate

For the year ended 31 December	BANK				GROUP			
	2017		2016		2017		2016	
	%	LKR 000	%	LKR 000	%	LKR 000	%	LKR 000
Tax using 28% tax rate on profit before tax (PBT)	**28.00**	**1,621,847**	28.00	1,235,788	**28.00**	**1,648,943**	28.00	1,308,767
Non-deductible expenses	**15.25**	**883,444**	16.64	734,605	**15.13**	**890,726**	15.94	745,177
Allowable deductions	**(5.01)**	**(290,324)**	(7.79)	(343,916)	**(4.97)**	**(292,919)**	(7.54)	(352,204)
Dividend income	**(3.66)**	**(212,156)**	(5.24)	(231,478)	**(3.60)**	**(212,156)**	(4.95)	(231,478)
Tax incentives	**(10.26)**	**(594,350)**	(7.36)	(324,683)	**(10.16)**	**(598,048)**	(6.95)	(324,973)
Taxable timing difference from capital allowances on assets	**(1.50)**	**(86,877)**	0.64	28,148	**(1.48)**	**(86,939)**	0.60	28,143
Tax losses from prior year	**–**	**–**	(1.61)	(71,270)	**(0.01)**	**(470)**	(1.53)	(71,651)
Adjustments	**–**	**–**	–	–	**0.67**	**39,597**	(0.37)	(17,135)
Current tax expense	**22.82**	**1,321,584**	23.28	1,027,194	**23.58**	**1,388,734**	23.20	1,084,646

21 Basic Earnings per Ordinary Share

Basic earnings per share of the Bank has been calculated by dividing the profit after income tax by the weighted average number of shares in issue during the financial year.

Basic group earnings per share has been calculated by dividing the profit after income tax attributable to the equity holders of the Bank by the weighted average number of shares in issue during the financial year.

Year ended 31 December	BANK		GROUP	
	2017 LKR 000	2016 LKR 000	**2017 LKR 000**	2016 LKR 000
Profit attributable to equity holders of the Bank (LKR '000)	**4,414,964**	3,288,723	**4,362,407**	3,414,980
Number of ordinary shares (Note 50)	**265,097,688**	265,097,688	**265,097,688**	265,097,688
Basic earnings per ordinary share – LKR	**16.65**	12.41	**16.46**	12.88

22 Dividend per Share

Dividend per share (LKR)

The Board of Directors of the Bank has approved the payment of a first and final dividend of LKR 5.00 per share for the year ended 31 December 2017.

23 *Analysis of Financial Instruments by Measurement Basis*

As at 31 December 2017	Fair value through profit or loss – mandatory LKR 000	Fair value held for trading LKR 000	Fair value through other comprehensive income LKR 000	Amortised cost LKR 000	Held to maturity LKR 000	Total LKR 000
23.1 Bank						
Financial Assets						
Cash and cash equivalents	–	–	–	4,106,225	–	4,106,225
Balances with Central Bank of Sri Lanka	–	–	–	10,557,688	–	10,557,688
Placements with banks	–	–	–	6,691,381	–	6,691,381
Derivative assets held-for-risk management	66,440	–	–	–	–	66,440
Other financial assets held for trading	–	310,922	–	–	–	310,922
Loans to and receivables from banks	–	–	–	10,984,266	–	10,984,266
Loans to and receivables from other customers	–	–	–	213,675,866	–	213,675,866
Financial investments	–	–	56,866,054	–	23,507,632	80,373,686
Due from subsidiaries	–	–	–	12,083	–	12,083
Government grant receivable	642,583	–	–	–	–	642,583
Other assets	–	–	–	2,775,741	–	2,775,741
	709,023	310,922	56,866,054	248,803,250	23,507,632	330,196,881
Financial Liabilities						
Due to banks	–	–	–	9,640,735	–	9,640,735
Derivative liabilities held-for-risk management	367,435	–	–	–	–	367,435
Due to other customers	–	–	–	193,307,534	–	193,307,534
Other borrowing	–	–	–	41,319,591	–	41,319,591
Debt securities issued	–	–	–	24,443,767	–	24,443,767
Subordinated term debt	–	–	–	9,202,870	–	9,202,870
Other liabilities	–	–	–	4,078,984	–	4,078,984
	367,435	–	–	281,993,481	–	282,360,916

As at 31 December 2016	Fair value through profit or loss – mandatory LKR 000	Fair value held for trading LKR 000	Fair value through other comprehensive income LKR 000	Amortised cost LKR 000	Held to maturity LKR 000	Total LKR 000

23.2 Bank

Financial Assets						
Cash and cash equivalents	–	–	–	4,330,934	–	4,330,934
Balances with Central Bank of Sri Lanka	–	–	–	8,062,567	–	8,062,567
Placements with banks	–	–	–	1,351,117	–	1,351,117
Derivative assets held-for-risk management	122,977	–	–	–	–	122,977
Loans to and receivables from banks	–	–	–	12,300,398	–	12,300,398
Loans to and receivables from other customers	–	–	–	185,784,979	–	185,784,979
Financial investments	–	–	49,272,243	–	23,189,085	72,461,328
Due from subsidiaries		–	–	19,855	–	19,855
Government grant receivable	861,915	–	–	–	–	861,915
Other assets	–	–	–	2,562,978	–	2,562,978
	984,892		49,272,243	214,412,828	23,189,085	287,859,048
Financial Liabilities						
Due to banks	–	–	–	18,103,587		18,103,587
Derivative liabilities held-for-risk management	105,741	–	–	–		105,741
Due to other customers	–	–	–	140,514,373		140,514,373
Other borrowing	–	–	–	40,751,346		40,751,346
Debt securities issued	–	–	–	29,179,185		29,179,185
Subordinated term debt	–	–	–	9,205,637		9,205,637
Other liabilities	–	–	–	3,850,825		3,850,825
	105,741	–	–	241,604,953	–	241,710,694

As at 31 December 2017	Fair value through profit or loss – mandatory LKR 000	Fair value held for trading LKR 000	Fair value through other comprehensive income LKR 000	Amortised cost LKR 000	Held to maturity LKR 000	Total LKR 000
23.3 Group						
Financial Assets						
Cash and cash equivalents	–	–	–	4,120,230	–	4,120,230
Balances with Central Bank of Sri Lanka	–	–	–	10,557,688	–	10,557,688
Placements with banks	–	–	–	6,712,131	–	6,712,131
Derivative assets held-for-risk management	66,440	–	–	–	–	66,440
Other financial assets held for trading	–	310,922	–	–	–	310,922
Loans to and receivables from banks	–	–	–	10,984,266	–	10,984,266
Loans to and receivables from other customers	–	–	–	213,675,866	–	213,675,866
Financial investments	–	–	56,866,054	–	23,507,632	80,373,686
Government grant receivable	642,583	–	–	–	–	642,583
Other assets	–	–	–	2,804,798	–	2,804,798
	709,023	310,922	56,866,054	248,854,979	23,507,632	330,248,610
Financial Liabilities						
Due to banks	–	–	–	9,640,735	–	9,640,735
Derivative liabilities held-for-risk management	367,435	–	–	–	–	367,435
Due to other customers	–	–	–	192,920,147	–	192,920,147
Other borrowing	–	–	–	41,290,874	–	41,290,874
Debt securities issued	–	–	–	24,443,767	–	24,443,767
Subordinated term debt	–	–	–	9,202,870	–	9,202,870
Other liabilities	–	–	–	4,195,940	–	4,195,940
	367,435	–	–	281,694,333	–	282,061,768

As at 31 December 2016	Fair value through profit or loss – mandatory LKR 000	Fair value held for trading LKR 000	Fair value through other comprehensive income LKR 000	Amortised cost LKR 000	Held to maturity LKR 000	Total LKR 000
23.4 Group						
Financial Assets						
Cash and cash equivalents	–	–	–	4,344,260	–	4,344,260
Balances with Central Bank of Sri Lanka	–	–	–	8,062,567	–	8,062,567
Placements with banks	–	–		1,415,985		1,415,985
Derivative assets held-for-risk management	122,977	–		–		122,977
Loans to and receivables from banks	–	–		12,300,398		12,300,398
Loans to and receivables from other customers	–	–	–	185,784,979		185,784,979
Financial investments	–	–	49,272,243	–	23,189,085	72,461,328
Government grant receivable	861,915	–	–	–	–	861,915
Other assets	–	–	–	2,609,655	–	2,609,655
	984,892	–	49,272,243	214,517,844	23,189,085	287,964,064
Financial Liabilities						
Due to banks	–	–	–	18,103,587	–	18,103,587
Derivative liabilities held-for-risk management	105,741			–	–	105,741
Due to other customers	–			140,219,872		140,219,872
Other borrowing	–			40,736,300		40,736,300
Debt securities issued	–			29,179,185		29,179,185
Subordinated term debt	–			9,205,637		9,205,637
Other liabilities	–			3,961,249		3,961,249
	105,741			241,405,830		241,511,571

24 *Cash and Cash Equivalents*

Accounting Policy →

For the purpose of the statement of cash flows, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with three months or less than three months' maturity from the date of acquisition.

Cash and cash equivalents include cash and short-term Treasury Bills with maximum three months' maturity from date of acquisition.

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

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Cash in hand	**3,603,883**	3,193,720	**3,617,888**	3,193,825
Balances with banks	**502,342**	1,137,214	**502,342**	1,150,435
	4,106,225	4,330,934	**4,120,230**	4,344,260

25 Balances with Central Bank of Sri Lanka

Accounting Policy →

Balances with Central Banks are carried at amortised cost in the statement of financial position.

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Statutory balances with Central Bank of Sri Lanka	**10,557,688**	8,062,567	**10,557,688**	8,062,567

As required by the provisions of Section 93 of Monetary Law Act, a minimum cash balance is maintained with the Central Bank of Sri Lanka. The minimum cash reserve requirement on rupee deposit liabilities is prescribed as a percentage of rupee deposit liabilities. The percentage is varied from time to time. Applicable minimum rate was 7.5%. There are no reserve requirement for deposit liabilities of the Foreign Currency Banking Unit and foreign currency deposit liabilities in the Domestic Banking Unit.

26 Placements with Banks

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Placements with Banks	**6,691,381**	1,351,117	**6,712,131**	1,415,985

27 Derivatives Held-for-Risk Management

Accounting Policy →

Derivative assets held-for-risk management purposes include all derivative assets that are not classified as trading assets and are measured at fair value in the statement of financial position.

Bank has not designated any derivative held-for-risk management purposes as a qualifying hedge relationship and therefore the Bank has not adopted hedge accounting.

Derivatives are classified as assets, when their fair value is positive or as liabilities, when their fair value is negative. Derivative assets and liabilities arising from different transactions are only offset, if the transactions are with the same counterparty, a legal right of offset exists, and the parties intend to settle the cash flows on a net basis.

27.1 Assets

As at		BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Forward foreign exchange contracts	– Currency Swaps	**65,552**	104,902	**65,552**	104,902
	– Other	**888**	18,075	**888**	18,075
		66,440	122,977	**66,440**	122,977

27.2 Liabilities

As at		BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Forward foreign exchange contracts	– Currency Swaps	**355,580**	94,327	**355,580**	94,327
	– Interest Rate Swaps	**6,028**	2,177	**6,028**	2,177
	– Other	**5,827**	9,237	**5,827**	9,237
		367,435	105,741	**367,435**	105,741

28 Other Financial Assets Held for Trading

Accounting Policy →

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*
- *they hold as a part of a portfolio that is managed together for short-term profit or position taking; or*

Financial assets Held-for-trading are recorded in the Statement of Financial Position at fair value. Changes in fair value are recognised in profit or loss. Interest and dividend income are recorded in 'Interest Income' and 'Net Gains/(Losses) from Trading' respectively in the Income Statement, according to the terms of the contract, or when the right to receive the payment has been established.

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Government of Sri Lanka Treasury bonds	**279,094**	–	**279,094**	–
Equity securities				
Quoted (Note 28.1)	**31,828**	–	**31,828**	–
	310,922	–	**310,922**	–

28.1 Quoted Ordinary Shares – Bank/Group

As at	31.12.2017 Number of ordinary shares	31.12.2017 Cost LKR 000	31.12.2017 Fair value LKR 000	31.12.2016 Number of ordinary shares	31.12.2016 Cost LKR 000	31.12.2016 Fair value LKR 000
Commercial Bank of Ceylon PLC – voting	**234,032**	**26,586**	**31,828**	–	–	–
		26,586	**31,828**		–	–

29 Loans to and Receivables from Banks

Accounting Policy →

Loans and receivables from Bank include amount due from Banks.

The carrying amount includes interest receivable from the Banks on these loans. This also includes investment by the Bank in any debentures, bonds, commercial paper or any other debt instrument which is not listed in the Colombo Stock Exchange or in any recognised market. The amount includes the principal amount and interest due and/or accrued on the date of the statement of financial position.

Principal amount of loans and advances (for example, over drawn balances in current account) are recognised when cash is advanced to a borrower. They are derecognised when either the borrower repays its obligations, or the loans are written off, or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less any reduction for impairment or uncollectibility.

	BANK		GROUP	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000
Gross loans and receivables	**10,984,266**	12,300,398	**10,984,266**	12,300,398
Allowance for impairment	–	–	–	–
Net loans and receivables	**10,984,266**	12,300,398	**10,984,266**	12,300,398

29.1 Analysis

29.1.1 By Product

	BANK 31.12.2017	BANK 31.12.2016	GROUP 31.12.2017	GROUP 31.12.2016
Refinanced Loans – Plantation development project	**27,977**	84,148	**27,977**	84,148
KFW* DFCC (V) SME in the North and East	–	2,940	–	2,940
Sri Lanka development bonds	**10,956,289**	12,213,310	**10,956,289**	12,213,310
Gross loans and receivables	**10,984,266**	12,300,398	**10,984,266**	12,300,398

** KFW – Kreditanstalt Fur Wiederaufbau*

29.1.2 By Currency

	BANK 31.12.2017	BANK 31.12.2016	GROUP 31.12.2017	GROUP 31.12.2016
Sri Lankan Rupee	**27,977**	87,088	**27,977**	87,088
United States Dollar	**10,956,289**	12,213,310	**10,956,289**	12,213,310
Gross loans and receivables	**10,984,266**	12,300,398	**10,984,266**	12,300,398

30 Loans to and Receivables from Other Customers

Accounting Policy →

Loans to and receivables from other customers include loans and advances and lease receivables of the Group.

The carrying amount includes capital and interest receivable from the customers on these loans. This also includes investment by the Bank in any debentures, bonds, commercial paper or any other debt instrument which is not listed in the Colombo Stock Exchange or in any recognised market. The amount includes the principal amount and interest due and/or accrued on the date of the statement of financial position.

Principal amount of loans and advances (for example, over drawn balances in current account) are recognised when cash is advanced to a borrower. They are derecognised when either the borrower repays its obligations, or the loans are written off, or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less any reduction for impairment or uncollectibility.

When the Bank is the lessor in a lease agreement that transfers substantially all of the risk and rewards incidental to the ownership of the asset to the lessee, the arrangement is classified as a finance lease and a receivable equal to the net investment in the lease is recognised and presented within loans and advances.

	BANK		GROUP	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000
Gross loans and receivables	**221,309,571**	192,454,529	**221,309,571**	192,454,529
Specific allowance for impairment (Note 30.2.1)	**(5,388,754)**	(4,778,752)	**(5,388,754)**	(4,778,752)
Collective allowance for impairment (Note 30.2.2)	**(2,244,951)**	(1,890,798)	**(2,244,951)**	(1,890,798)
Net loans and receivables	**213,675,866**	185,784,979	**213,675,866**	185,784,979

30.1 Analysis

30.1.1 By Product

Overdrafts	**40,204,544**	29,115,220	**40,204,544**	29,115,220
Trade finance	**29,778,452**	24,726,990	**29,778,452**	24,726,990
Lease rentals receivable (Note 30.1.1.1)	**16,493,374**	15,909,152	**16,493,374**	15,909,152
Credit cards	**276,432**	242,091	**276,432**	242,091
Pawning	**2,597,441**	2,109,667	**2,597,441**	2,109,667
Staff loans	**1,544,400**	1,397,579	**1,544,400**	1,397,579
Term loans	**129,086,941**	116,395,228	**129,086,941**	116,395,228
Commercial papers and asset back notes	**1,140,487**	962,763	**1,140,487**	962,763
Debenture loans	**–**	71,119	**–**	71,119
Preference shares unquoted	**187,500**	517,500	**187,500**	517,500
Securities purchased under resale agreements	**–**	1,007,220	**–**	1,007,220
Gross loans and receivables	**221,309,571**	192,454,529	**221,309,571**	192,454,529

As at	BANK		GROUP	
	31.12.2017 LKR 000	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000

30.1.1.1 Lease rentals receivable

Gross investment in leases:				
Lease rentals receivable				
– within one year	**8,167,382**	7,260,287	**8,167,382**	7,260,287
– one to five years	**11,774,307**	11,667,471	**11,774,307**	11,667,471
	19,941,689	18,927,758	**19,941,689**	18,927,758
Less: Deposit of rentals	**12,551**	11,480	**12,551**	11,480
Unearned income on rentals receivable				
– within one year	**1,720,165**	1,483,826	**1,720,165**	1,483,826
– one to five years	**1,715,599**	1,523,300	**1,715,599**	1,523,300
	16,493,374	15,909,152	**16,493,374**	15,909,152

30.1.2 By Currency

Sri Lankan Rupee	**199,579,777**	175,840,682	**199,579,777**	175,840,682
United States Dollar	**20,885,187**	16,021,231	**20,885,187**	16,021,231
Great Britain Pound	**511,472**	428,982	**511,472**	428,982
Australian Dollar	**16,099**	18,140	**16,099**	18,140
Euro	**317,036**	145,494	**317,036**	145,494
Gross loans and receivables	**221,309,571**	192,454,529	**221,309,571**	192,454,529

30.1.3 By Industry

Agriculture and fishing	**22,513,650**	21,177,351	**22,513,650**	21,177,351
Manufacturing	**50,116,479**	42,467,362	**50,116,479**	42,467,362
Tourism	**13,818,386**	11,345,823	**13,818,386**	11,345,823
Transport	**7,022,585**	6,561,001	**7,022,585**	6,561,001
Construction	**25,916,910**	14,769,286	**25,916,910**	14,769,286
Trading	**44,461,385**	42,917,888	**44,461,385**	42,917,888
Financial and business services	**9,856,842**	8,285,786	**9,856,842**	8,285,786
Infrastructure	**15,160,210**	13,767,614	**15,160,210**	13,767,614
Other services	**14,819,671**	14,643,050	**14,819,671**	14,643,050
Consumer durables	**8,006,853**	8,096,930	**8,006,853**	8,096,930
New economy	**1,585,722**	1,399,681	**1,585,722**	1,399,681
Others	**8,030,878**	7,022,757	**8,030,878**	7,022,757
Gross loans and receivables	**221,309,571**	192,454,529	**221,309,571**	192,454,529

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

30.2 Movements in Specific and Collective Allowance for Impairment

30.2.1 Specific Allowance for Impairment

Balance at beginning	**4,778,752**	4,240,756	**4,778,752**	4,240,756
Charge to income statement	**724,402**	792,389	**724,402**	792,389
Effect of foreign currency movement	**21,782**	22,903	**21,782**	22,903
Write-off of loans and receivables	**(136,182)**	(277,296)	**(136,182)**	(277,296)
Balance on 31 December	**5,388,754**	4,778,752	**5,388,754**	4,778,752

30.2.2 Collective Allowance for Impairment

Balance at beginning	**1,890,798**	1,924,882	**1,890,798**	1,924,882
Charge to income statement	**405,973**	81,772	**405,973**	81,772
Effect of foreign currency movement	**382**	3,712	**382**	3,712
Transfer to dues on terminated leases*	**(4,671)**	(3,344)	**(4,671)**	(3,344)
Write-off of loans and receivables	**(47,531)**	(116,224)	**(47,531)**	(116,224)
Balance on 31 December	**2,244,951**	1,890,798	**2,244,951**	1,890,798
Total	**7,633,705**	6,669,550	**7,633,705**	6,669,550

** Included in debtors in other assets Note 43.*

31 Financial Investments – Available for Sale

Accounting Policy →

Available-for-sale investments are non-derivative investments that were designated as available for sale or not classified as another category of financial assets. These include Treasury Bills, Bonds, Debt Securities and unquoted and quoted equity securities. They are carried at fair value except for unquoted equity securities whose fair value cannot reliably be measured and therefore carried at cost.

Interest income is recognised in profit or loss, using the effective interest method. Dividend income was recognised in profit or loss when the Bank become entitled to the dividend.

Fair value changes are recognised in other comprehensive income until the investment is sold or impaired, where upon the cumulative gains and losses previously recognised in other comprehensive income are reclassified to profit or loss as are classification adjustment.

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Government of Sri Lanka Treasury bills	**19,484,244**	16,993,057	**19,484,244**	16,993,057
Government of Sri Lanka Treasury bonds	**18,261,795**	12,372,198	**18,261,795**	12,372,198
Equity securities				
Quoted (Note 31.1)	**18,195,008**	18,797,640	**18,195,008**	18,797,640
Unquoted (Note 31.2)	**85,555**	112,484	**85,555**	112,484
Preference shares (Note 31.3)	**500**	500	**500**	500
Quoted units in Unit Trust (Note 31.4)	**194,590**	190,153	**194,590**	190,153
Unquoted units in Unit Trust (Note 31.5)	**644,362**	806,211	**644,362**	806,211
Total	**56,866,054**	49,272,243	**56,866,054**	49,272,243

All the financial investments are carried at fair value except for unquoted equity securities and irredeemable preference shares whose fair value cannot reliably be measured is carried at cost.

As at	31.12.2017			31.12.2016		
	Number of ordinary shares	Cost* LKR 000	Fair value LKR 000	Number of ordinary shares	Cost* LKR 000	Fair value LKR 000
31.1 Quoted Ordinary Shares						
Banks, finance and insurance						
Commercial Bank of Ceylon PLC – voting	**126,696,192**	**4,839,953**	**17,230,682**	122,747,994	3,508,069	17,798,459
Commercial Bank of Ceylon PLC – non-voting	**257,805**	**20,790**	**27,070**	230,726	18,246	26,649
National Development Bank PLC	**2,076,280**	**364,017**	**283,412**	2,000,000	352,369	312,000
		5,224,760	**17,541,164**		3,878,684	18,137,108
Beverages, Food and Tobacco						
Ceylon Tobacco Company PLC	**34,532**	**1,949**	**33,154**	59,532	3,360	47,626
		1,949	**33,154**		3,360	47,626
Chemicals and Pharmaceuticals						
Chemical Industries (Colombo) PLC – voting	**247,900**	**14,131**	**16,535**	247,900	14,131	22,311
Chemical Industries (Colombo) PLC – non-voting	**389,400**	**15,577**	**20,249**	389,400	15,577	26,479
		29,708	**36,784**		29,708	48,790
Construction and Engineering						
Access Engineering PLC	**473,000**	**9,737**	**11,163**	473,000	9,737	11,730
Colombo Dockyard PLC	**160,000**	**12,160**	**14,048**	160,000	12,160	12,160
		21,897	**25,211**		21,897	23,890
Diversified Holdings						
Carson Cumberbatch PLC	**46,967**	**7,745**	**8,454**	46,967	12,681	8,360
Hayleys PLC	**7,333**	**2,225**	**1,760**	7,333	2,225	1,980
Hemas Holdings PLC	**496,560**	**16,297**	**62,567**	496,560	16,297	49,159
John Keells Holdings PLC	**219,907**	**18,362**	**32,700**	219,907	18,362	31,886
Melstacorp Limited	**1,669,940**	**69,829**	**99,361**	1,669,940	69,829	100,196
Richard Pieris & Co. PLC	**612,956**	**5,047**	**7,907**	1,000,000	8,234	8,100
		119,505	**212,749**		127,628	199,681
Healthcare						
Ceylon Hospitals PLC – voting	**100,000**	**2,306**	**8,300**	100,000	2,306	8,740
Ceylon Hospitals PLC – non-voting	**240,000**	**4,167**	**15,672**	240,000	4,167	17,976
		6,473	**23,972**		6,473	26,716
Hotels and Travels						
Dolphin Hotels PLC	**100,000**	**964**	**2,900**	100,000	964	3,940
		964	**2,900**		964	3,940

Sector classification and fair value per share are based on the list published by Colombo Stock Exchange, as at the reporting date.

** Cost is reduced by write-off of diminution in value other than temporary in respect of investments.*

As at	31.12.2017			31.12.2016		
	Number of ordinary shares	Cost* LKR 000	Fair value LKR 000	Number of ordinary shares	Cost* LKR 000	Fair value LKR 000
Investment Trusts						
Ceylon Guardian Investment Trust PLC	**152,308**	**5,918**	**13,251**	152,308	5,918	17,058
Ceylon Investment PLC	**288,309**	**9,428**	**12,887**	288,309	9,429	14,704
		15,346	**26,138**		15,347	31,762
Telecommunications						
Dialog Axiata PLC	**2,050,000**	**18,860**	**26,855**	2,050,000	18,860	21,525
Manufacturing						
ACL Cables PLC	**40,000**	**2,278**	**1,688**	–	–	–
Ceylon Grain Elevators PLC	**148,997**	**9,197**	**9,834**	48,997	1,297	4,042
Chevron Lubricants Lanka PLC	**761,628**	**27,907**	**90,634**	761,628	27,907	119,576
Kelani Tyres PLC	**75,000**	**4,538**	**3,330**	–	–	–
Piramal Glass Ceylon PLC	**5,000,000**	**14,024**	**29,000**	5,000,000	14,024	26,500
Royal Ceramics Lanka PLC	**139,800**	**16,996**	**16,007**	139,800	16,996	16,217
Teejay Lanka PLC	**75,000**	**3,141**	**2,550**	–	–	–
Tokyo Cement Company (Lanka) PLC – voting	**120,000**	**5,734**	**7,920**	100,000	5,734	5,950
Tokyo Cement Company (Lanka) PLC – non-voting	**1,472,515**	**25,759**	**86,878**	1,227,096	25,759	63,196
	–	**109,574**	**247,841**		91,717	235,481
Power & Energy						
Vallibel Power Erathna PLC	**2,400,000**	**6,400**	**18,240**	2,400,000	6,400	21,120
		6,400	**18,240**		6,400	21,120
Total quoted ordinary shares – Bank		**5,555,436**	**18,195,008**		4,201,038	18,797,640
Commercial Bank of Ceylon PLC – Equity Adjustment		**2,297,772**	**–**		2,499,357	–
Total quoted ordinary shares – Group		**7,853,208**	**18,195,008**		6,700,395	18,797,640

Sector classification and fair value per share are based on the list published by Colombo Stock Exchange, as at the reporting date.

** Cost is reduced by write-off of diminution in value other than temporary in respect of Investments.*

As at	31.12.2017		31.12.2016	
	Number of ordinary shares	**Cost* LKR 000**	Number of ordinary shares	Cost* LKR 000
31.2 Unquoted Ordinary Shares				
Credit Information Bureau of Sri Lanka	**9,184**	**918**	9,184	918
Durdans Medical & Surgical Hospital (Pvt) Limited	**1,273,469**	**16,029**	1,273,469	16,029
Fitch Ratings Lanka Limited	**62,500**	**625**	62,500	625
Lanka Clear (Private) Limited	**100,000**	**1,000**	100,000	1,000
Lanka Financial Services Bureau Limited	**100,000**	**1,000**	100,000	1,000
Samson Reclaim Rubber Limited	**116,700**	**–**	116,700	2,334
Sinwa Holdings Limited	**–**	**–**	460,000	9,200
Society for Worldwide Interbank Financial Telecommunication	**6**	**3,385**	6	3,385
Sun Tan Beach Resorts Limited	**9,059,013**	**62,598**	9,059,013	67,943
The Video Team (Private) Limited	**30,000**	**–**	30,000	300
Wayamba Plantations (Private) Limited	**–**	**–**	2,750,000	9,750
Total unquoted ordinary shares – Bank/Group		**85,555**		112,484

* *Cost is reduced by write-off of diminution in value other than temporary in respect of investments.*

As at	31.12.2017			31.12.2016		
	Number of ordinary shares	**Cost LKR 000**	**Fair value LKR 000**	Number of ordinary shares	Cost LKR 000	Fair value LKR 000
31.3 Unquoted Irredeemable Preference Shares						
Arpico Finance Company PLC	**50,000**	**500**	**500**	50,000	500	500
Total investments in unquoted irredeemable preference shares – Bank/Group		**500**	**500**		500	500

As at	31.12.2017			31.12.2016		
	Number of units	**Cost LKR 000**	**Fair value LKR 000**	Number of units	Cost LKR 000	Fair value LKR 000
31.4 Quoted Units in Unit Trust						
NAMAL Acuity Value Fund	**2,112,810**	**106,070**	**194,590**	2,112,810	106,070	190,153
Total investments in quoted unit – Bank/Group		**106,070**	**194,590**		106,070	190,153

As at	31.12.2017 Number of units	31.12.2017 Cost LKR 000	31.12.2017 Fair value LKR 000	31.12.2016 Number of units	31.12.2016 Cost LKR 000	31.12.2016 Fair value LKR 000

31.5 Unquoted Units in Unit Trust

NAMAL Growth Fund	**2,125,766**	**251,539**	**288,256**	2,125,766	251,539	272,867
NAMAL Income Fund	**5,810,424**	**59,322**	**80,778**	11,162,129	113,961	143,719
NAMAL Money Market Fund	–	–	–	11,679,366	118,457	125,616
National Equity Fund	**250,000**	**2,657**	**8,417**	250,000	2,657	8,352
Guardian Acuity Equity Fund	**9,052,505**	**150,000**	**154,486**	9,052,504	150,000	151,432
JB Vantage Value Equity Fund	**5,224,660**	**100,000**	**112,425**	5,224,660	100,000	104,225
Total investments in unquoted unit trusts – Bank/Group		**563,518**	**644,362**		736,614	806,211

As at	Ordinary Shares Quoted LKR 000	Ordinary Shares Unquoted LKR 000	Preference Unquoted LKR 000	Unit Trusts Quoted LKR 000	Unit Trusts Unquoted LKR 000	Total 31.12.2017 LKR 000	Total 31.12.2016 LKR 000

31.6 Equity Securities

31.6.1 Composition *

31.6.1.1 Bank

Performing investments	18,180,960	22,957	500	194,590	356,107	**18,755,114**	19,556,127
Non-performing investments	14,048	62,598	–	–	288,255	**364,901**	350,860
	18,195,008	85,555	500	194,590	644,362	**19,120,015**	19,906,987

31.6.1.2 Group

Performing investments	18,180,960	22,957	500	194,590	356,107	**18,755,114**	19,556,127
Non-performing investments	14,048	62,598	–	–	288,255	**364,901**	350,860
	18,195,008	85,555	500	194,590	644,362	**19,120,015**	19,906,987

** Disclosure as per the direction on the prudential norms for classification, valuation and operation of the Bank's investment portfolio.*

32 Financial Investments – Held-to-maturity

Accounting Policy →

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that Bank positively intends, and is able, to hold to maturity. Held-to-maturity investments are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest rate method, less any impairment losses.

A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in there classification of all investment securities as available for sale for the current and the subsequent two financial years.

However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- *Sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;*
- *Sales or reclassifications after the Bank has collected substantially all of the asset's original principal; and*
- *Sales or reclassifications attributable to non-recurring isolated events beyond the Group's control that could not have been reasonably anticipated.*

	BANK		GROUP	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000
Quoted debentures (Note 32.1)	**5,131,404**	5,949,747	**5,131,404**	5,949,747
Sri Lanka Government Securities				
Treasury Bills	**941,938**	2,357,188	**941,938**	2,357,188
Treasury Bonds	**17,434,290**	14,882,150	**17,434,290**	14,882,150
Total	**23,507,632**	23,189,085	**23,507,632**	23,189,085

As at	**31.12.2017**		31.12.2016	
	Number of debentures	**Cost of investment LKR 000**	**Number of debentures**	**Cost of investment** LKR 000
32.1 Quoted Debentures				
Abans Limited	–	–	2,500,000	267,917
Access Engineering PLC	**2,500,000**	**253,031**	2,500,000	253,031
Alliance Finance Company PLC	**4,221,693**	**461,755**	5,721,693	623,823
Central Finance Company PLC	**1,793,900**	**191,604**	2,075,700	221,626
Commercial Credit & Finance PLC	**4,500,000**	**461,913**	4,500,000	461,879
HDFC Bank	–	–	532,200	55,227
Hemas Holdings PLC	**827,900**	**85,055**	827,900	85,049
Lanka Orix Leasing Company PLC	**3,000,000**	**306,806**	3,000,000	306,787
LB Finance PLC	**1,155,200**	**116,344**	–	–
Lion Brewery (Ceylon) PLC	**1,440,900**	**173,420**	1,462,200	195,446
People's Leasing and Finance PLC	**13,326,300**	**1,391,594**	13,326,300	1,391,578
Richard Pieris and Company PLC	–	–	1,201,000	123,303
Senkadagala Finance PLC	**3,650,000**	**371,981**	3,650,000	371,981
Singer (Sri Lanka) PLC	**6,441,900**	**668,738**	8,975,800	942,964
Siyapatha Finance Limited	**2,000,000**	**217,802**	2,000,000	217,802
Softlogic Finance PLC	**706,500**	**72,431**	706,500	72,429
Vallibel Finance PLC	**3,500,000**	**358,930**	3,500,000	358,905
Total investments in quoted debentures – Bank/Group		**5,131,404**		5,949,747

33 Investments in Subsidiaries

Accounting Policy →

Bank's investments in subsidiaries are stated at cost less impairment losses. Reversals of impairment losses are recognised in the income statement, if there has been a change in the estimates used to determine the recoverable amount of the investment.

As at	DFCC Consulting (Pvt) Limited ownership 100% LKR 000	Lanka Industrial Estates Limited ownership 51.16% LKR 000	Synapsys Limited ownership 100% LKR 000	BANK **31.12.2017** **LKR 000**	BANK 31.12.2016 LKR 000
Balance at beginning	5,000	97,036	70,000	**172,036**	172,036
Investments during the year	–	–	65,000	**65,000**	–
Less: Allowance for impairment (Note 33.1)	–	–	70,000	**70,000**	60,104
Balance net of impairment at the end	5,000	97,036	65,000	**167,036**	111,932

33.1 Movements in Impairment Allowance

Balance at beginning	60,104	39,181
Charge to income statement	9,896	20,923
Balance on 31 December	70,000	60,104

Investment in Synapsys Limited is classified as non-performing (no dividend for three consecutive years).

33.2 Non-Controlling Interest (NCI) in Subsidiaries

Accounting Policy →

The Non-Controlling Interest are measured at their proportionate share of the acquiree's identifiable net assets at the date of acquisition. Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

	Percentage of ownership interest held by NCI	Percentage of voting rights held by NCI	Share of total comprehensive income of NCI for the year ended		NCI as at		Dividends paid to NCI for the year ended	
	31.12.2017 %	31.12.2016 %	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000
Lanka Industrial Estates Limited	**48.84**	48.84	**71,572**	54,270	**276,872**	259,900	**54,600**	46,796
			71,572	54,270	**276,872**	259,900	**54,600**	46,796

33.3 Summarised Financial Information of Subsidiaries

Lanka Industrial Estates Limited

As at	31.12.2017 LKR 000	31.12.2016 LKR 000
Assets	**782,569**	702,868
Liabilities	**215,730**	170,777
Equity	**566,839**	532,091
For the year ended		
Revenue	**322,161**	293,687
Profit after tax	**146,078**	110,748
Other comprehensive income	**456**	361
Total comprehensive income	**146,534**	111,109

34 *Investments in Associate (Unquoted)*

Accounting Policy →

Investments in associates are recognised using the equity method, initially stated at cost, including attributable goodwill, and are adjusted thereafter for the post-acquisition change in Bank's share of net assets.

Unrealised gains on transactions between Bank and its associates are eliminated to the extent of Bank's interest in the respective associate. Unrealised losses are also eliminated to the extent of Bank's interest in the associate.

	BANK		GROUP	
As at	31.12.2017 LKR 000	31.12.2016 LKR 000	31.12.2017 LKR 000	31.12.2016 LKR 000
National Asset Management Limited (Ownership 30%)				
Balance at beginning	**35,270**	35,270	**64,873**	66,980
Share of profit after tax	**–**	–	**9,414**	11,752
Share of other comprehensive income/(expenses)	**–**	–	**479**	(3,359)
Dividend received – Elimination on consolidation	**–**	–	**(7,500)**	(10,500)
Balance on 31 December	**35,270**	35,270	**67,266**	64,873

34.1 Summarised Financial Information of Associate

National Asset Management Limited

As at	31.12.2017 LKR 000	31.12.2016 LKR 000
Assets	**238,743**	239,051
Liabilities	**14,576**	22,861
Equity	**224,167**	216,190
For the year ended		
Revenue	**128,102**	134,075
Profit after tax	**31,380**	39,174
Other comprehensive income/(expenses)	**1,596**	(11,198)
Total comprehensive income	**32,976**	27,976

35 Investments in Joint Venture (Unquoted)

Accounting Policy →

Investments in Joint Ventures are recognised using the equity method, initially stated at cost, including attributable goodwill, and are adjusted thereafter for the post-acquisition change in Bank's share of net assets.

Unrealised gains on transactions between Bank and its Joint Ventures are eliminated to the extent of Bank's interest in the respective Joint Ventures. Unrealised losses are also eliminated to the extent of Bank's interest in the Joint Ventures.

As at	**31.12.2017 Cost of investment LKR 000**	31.12.2016 Cost of investment LKR 000
35.1 Investments in Joint Venture – Bank		
Acuity Partners (Pvt) Limited (ownership 50%)	**755,000**	755,000
	755,000	755,000

As at	**31.12.2017 LKR 000**	**31.12.2016 LKR 000**
35.2 Investment in Joint Venture – Group		
Share of identifiable asset and liabilities of joint venture as at the beginning of the year	**1,562,942**	1,365,507
Share of unrealised profit on disposal of investments	**(184,688)**	(184,688)
Balance at beginning	**1,378,254**	1,180,819
Investment made during the year	**–**	100,000
Share of profit net of tax	**175,616**	149,399
Share of other comprehensive income	**(21,416)**	(21,154)
Change in holding – through subsidiary of joint venture	**117,478**	(610)
Dividend received during the year	**(33,220)**	(30,200)
Group's share of net assets	**1,616,711**	1,378,254

35.3 Summarised Financial Information of Joint Venture – Acuity Partners (Pvt) Limited

For the year ended	**31.12.2017 Cost of investment LKR 000**	31.12.2016 Cost of investment LKR 000
Revenue	**808,127**	671,603
Depreciation	**48,601**	34,654
Income tax expense	**50,241**	61,499
Profit after tax	**564,879**	534,885
Other comprehensive expenses	**(69,456)**	(48,143)
Total comprehensive income	**495,423**	486,742

As at	31.12.2017 LKR 000	31.12.2016 LKR 000
Current assets	**5,241,692**	4,085,610
Non-current assets	**9,299,827**	7,488,394
Current liabilities	**7,688,029**	6,098,931
Non-current liabilities	**1,025,766**	1,063,494

	BANK	
As at	31.12.2017 LKR 000	31.12.2016 LKR 000

36 Due from Subsidiaries

DFCC Consulting (Pvt) Limited	**906**	2,265
Synapsys Limited	**11,177**	17,590
	12,083	19,855

37 Investment Property

Accounting Policy →

Investment property of the Group (held by Subsidiary Lanka Industrial Estates Limited) is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business. The Group has chosen the cost model instead of fair value model and therefore investment property is measured at cost. Cost includes expenditure that is directly attributable to the acquisition of the investment property.

Any gain or loss on disposal of an investment property (calculated as the difference between the next proceeds from disposal and the carrying amount of the item) is recognised in the Income Statement.

	GROUP	
As at	31.12.2017 LKR 000	31.12.2016 LKR 000
Cost		
Balance at beginning	**363,329**	313,909
Acquisition	**165,336**	49,420
Transfers	**(64,317)**	–
Cost as at 31 December	**464,348**	363,329
Less: Accumulated Depreciation		
Balance at beginning	**131,977**	118,177
Charge for the year	**13,718**	13,800
Accumulated depreciation as at 31 December	**145,695**	131,977
Carrying amount as at 31 December	**318,653**	231,352

As at 31 December 2017	Buildings sq.ft	Extent of Land perches*	Cost LKR 000	Accumulated depreciation/ impairment LKR 000	Net Book value LKR 000	Fair value LKR 000
37.1 Details of Investment Properties						
Pattiwila Road, Sapugaskanda, Makola	280,000	20,000	464,348	145,695	318,653	2,344,314

** 1 Perch = 25.2929 m²; 1 Sq. ft = 0.0929 m²*

The fair value of investment property as at 31 December 2017 situated at Pattiwila Road, Sapugaskanda, Makola was based on market valuations carried out in December 2016 by Mr P B Kalugalagedara, Fellow Members of Institute of Valuers (Sri Lanka), Chartered Valuer.

Rental income from investment property of Group for 2017, LKR 225 million (2016 – LKR 198 million).
Operating expenses on investment property of Group for 2017 – LKR 29 million (2016 – LKR 28 million).

38 Property, Plant and Equipment

Accounting Policy →

Recognition and Measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset.

Any gain or loss on disposal of an item of property, plant and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in the income statement.

Subsequent Costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Bank. Ongoing repairs and maintenance costs are expensed as incurred.

Capital work-in-Progress

These are expenses of a capital nature directly incurred in the construction of buildings, major plant and machinery and system development, awaiting capitalisation. These are stated in the Statement of Financial Position at cost. Capital work-in-progress would be transfered to the relevant asset when it is available for use i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Capital work-in-progress is stated at cost less any accumulated impairment losses.

Depreciation

Items of property, plant and equipment are depreciated from the month they are available for use up to the month of disposal. Depreciation is calculated to write-off the cost of items of property, plant and equipment less their estimated residual values using the straight-line basis over their estimated useful lives. Land is not depreciated.

The estimated useful lives for the current and comparative periods of significant items of property, plant and equipment are as follows:

	Years
Buildings	**20**
Office equipment and motor vehicles	**5**
Fixtures and fittings	**10**

Derecognition

The carrying amount of property and equipment is derecognised on disposal or when no-future economic benefits are expected from its use of the gain or loss arising from the derecognition (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in the income statement.

	Land and buildings LKR 000	Office equipment LKR 000	Furniture and fittings LKR 000	Motor vehicles LKR 000	**Total 31.12.2017 LKR 000**	Total 31.12.2016 LKR 000

38.1 Composition: Bank

	Land and buildings LKR 000	Office equipment LKR 000	Furniture and fittings LKR 000	Motor vehicles LKR 000	**Total 31.12.2017 LKR 000**	Total 31.12.2016 LKR 000
Cost at beginning	467,861	1,573,810	840,181	269,276	**3,151,128**	2,947,897
Acquisitions	11,324	486,099	85,664	22,210	**605,297**	218,550
Less: Disposals	–	16,228	911	30,404	**47,543**	15,319
Cost as at 31 December	479,185	2,043,681	924,934	261,082	**3,708,882**	3,151,128
Accumulated depreciation at beginning	214,541	1,238,231	524,366	246,133	**2,223,271**	2,004,880
Depreciation for the years	18,833	158,558	67,820	14,337	**259,548**	233,079
Less: Accumulated depreciation on disposals	–	16,183	599	30,405	**47,187**	14,688
Accumulated depreciation as at 31 December	233,374	1,380,606	591,587	230,065	**2,435,632**	2,223,271
Carrying amount as at 31 December	245,811	663,075	333,347	31,017	**1,273,250**	927,857

38.1.1 List of Freehold Land and Buildings

As at 31 December 2017	Buildings Sq. Ft.	Extent of land Perches*	Cost LKR 000	Accumulated depreciation LKR 000	Net book value LKR 000
73/5, Galle Road, Colombo 3	57,190	106.81	85,518	75,716	9,802
5, Deva Veediya, Kandy	6,260	12.54	16,195	7,408	8,787
259/30, Kandy Road, Bambarakelle, Nuwara-Eliya	–	93.5	7,279	–	7,279
73, W A D Ramanayake Mawatha, Colombo 2	37,538	45.00	197,268	132,537	64,731
4 A, 4th Cross Lane, Borupana, Ratmalana	–	20.00	2,600	–	2,600
454, Main Street, Negombo	19,087	29.00	170,325	17,713	152,612
			479,185	233,374	245,811

** 1 perch = 25.2929m²; 1 sq ft = 0.0929m²*

38.1.2 Market Value of Properties

	LKR million	Date of valuation
73/5, Galle Road, Colombo 3	1,509	31.12.2017
5, Deva Veediya, Kandy	125	31.12.2017
73, W A D Ramanayake Mawatha, Colombo 2	705	31.12.2017
4 A, 4th Cross Lane, Borupana, Ratmalana	15	31.12.2017
454, Main Street, Negombo	250	05.05.2015
259/30, Kandy Road, Bambarakelle, Nuwara-Eliya	80	26.05.2015

(Valued by Mr A A M Fathihu – Former Government Chief Valuer and Mr J S M I B Karunatilaka, Associate Member of the Institute of Valuers of Sri Lanka).

38.1.3 Fully-Depreciated Property, Plant and Equipment – Bank

The initial cost of fully-depreciated property, plant and equipment as at 31 December 2017, which are still in use as at the reporting date is as follows:

	BANK	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000
Buildings	**79,312**	58,739
Office equipment	**1,007,584**	909,043
Furniture and fittings	**267,954**	158,184
Motor vehicles	**199,691**	183,925
	1,554,541	1,309,891

	Land & buildings LKR 000	Office equipment LKR 000	Furniture & fittings LKR 000	Motor vehicles LKR 000	**Total 31.12.2017 LKR 000**	Total 31.12.2016 LKR 000
38.2 Composition – Group						
Cost at beginning	691,570	1,620,996	853,094	320,850	**3,486,510**	3,254,738
Acquisitions	18,492	488,220	86,390	22,210	**615,312**	258,492
Less: Disposals	–	16,799	911	30,651	**48,361**	26,360
Write-off	–	–	–	–	**–**	360
Cost as at 31 December	710,062	2,092,417	938,573	312,409	**4,053,461**	3,486,510
Accumulated depreciation at beginning	356,983	1,268,873	541,168	276,867	**2,443,891**	2,212,437
Depreciation for the year	31,092	164,642	68,811	21,879	**286,424**	257,532
Less: Accumulated depreciation on disposals	–	16,764	599	30,652	**48,015**	25,718
Write-off	–	–	–	–	**–**	360
Accumulated depreciation as at 31 December	388,075	1,416,751	609,380	268,094	**2,682,300**	2,443,891
Carrying amount as at 31 December	321,987	675,666	329,193	44,315	**1,371,161**	1,042,619

39 Intangible Assets

Accounting Policy →

Intangible Assets – Computer Application Software

All software licensed for use by the Bank, not constituting an integral part of related hardware are included in the statement of financial position under the category intangible assets and carried at cost less cumulative amortisation and any impairment losses.

The initial acquisition cost comprises licence fee paid at the inception, import duties, non-refundable taxes and levies, cost of customising the software to meet the specific requirements of the Bank and other directly attributable expenditure in preparing the asset for its intended use.

The initial cost is enhanced by subsequent expenditure incurred by further customisation to meet ancillary transaction processing and reporting requirements tailor-made for the use of the Bank constituting an improvement to the software.

The cost is amortised, using the straight-line method, at the rate of 20% per annum commencing from the date the application software is available-for-use. The amortised amount is based on the best estimate of its useful life, such that the cost is amortised fully at the end of the useful life during which the Bank has legal right of use. The amortisation cost is recognised as an expense.

An intangible asset is derecognised on disposal or when no future economic benefits are expected from its use and subsequent disposal.

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Software (refer 39.1)	**369,777**	203,742	**374,104**	208,382
Software under development (refer 39.2)	**128,307**	–	**128,307**	–
Total	**498,084**	203,742	**502,411**	208,382

39.1 Software

Cost at beginning	**1,024,450**	1,313,816	**1,031,330**	1,316,581
Acquisitions	**275,608**	58,833	**276,529**	62,948
Less: Write-off*	–	348,199	–	348,199
Cost as at 31 December	**1,300,058**	1,024,450	**1,307,859**	1,031,330
Accumulated amortisation at beginning	**820,708**	1,066,701	**822,948**	1,068,636
Amortisation for the year	**109,573**	98,262	**110,807**	98,567
Less: Write-off*	–	344,255	–	344,255
Accumulated amortisation as at 31 December	**930,281**	820,708	**933,755**	822,948
Carrying amount as at 31 December	**369,777**	203,742	**374,104**	208,382

** Software not in use*

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

39.2 Software Under Development

As at begining	–	–	–	–
Addition to working progress	**128,307**	–	**128,307**	–
Transfers/adjustments	–	–	–	–
As at 31 December	**128,307**	–	**128,307**	–

40 Goodwill on Consolidation

Accounting Policy →

Goodwill arises on the acquisition of subsidiaries, when the aggregate of the fair value of the consideration transferred, the amount of any non-controlling interest and the fair value of any previously held equity interest in the acquire exceed the amount of the identifiable assets and liabilities acquired. If the amount of the identifiable assets and liabilities acquired is greater, the difference is recognised immediately in the income statement. Goodwill arises on the acquisition of interests in joint ventures and associates when the cost of investment exceeds Bank's share of the net fair value of the associate's or joint venture's identifiable assets and liabilities.

As at	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
DFCC Vardhana Bank PLC	**146,603**	146,603
Lanka Industrial Estates Limited	**9,623**	**9,623**
	156,226	156,226

In accordance with the provisions of part VIII of the Companies Act, DFCC Vardhana Bank PLC (DVB) has been amalgamated with DFCC Bank PLC with effect from 1 October 2015. The amalgamation between two entities is considered as a common control transaction, as DFCC Bank continues to control the operations of DVB after amalgamation. Thus the results of amalgamation of two entities are economically the same before and after the amalgamation as the entity will have identical net assets. Therefore, DFCC will continue to record carrying values including the remaining goodwill that resulted from the original acquisition of DVB in the consolidated financial status.

41 Government Grant Receivable/Deferred Income – CBSL Swap

Accounting Policy →

Government grants are recognised initially as deferred income at fair value, when there is a reasonable assurance that they will be received and Group will comply with the conditions associated with the grant, and are then recognised in profit or loss as other income on a systematic basis in the period in which the expenses (losses) are recognised.

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
41.1 Government Grant – Receivable				
Fair value at beginning	**861,915**	539,758	**861,915**	539,758
Change in fair value on the renewal of contract	**(133,055)**	405,763	**(133,055)**	405,763
Change in fair value during the year	**(86,277)**	(83,606)	**(86,277)**	(83,606)
Fair value at 31 December	**642,583**	861,915	**642,583**	861,915
41.2 Government Grant – Deferred Income				
Fair value at beginning	**701,665**	476,008	**701,665**	476,008
Change in fair value on the renewal of contract	**(133,055)**	405,763	**(133,055)**	405,763
Change in fair value during the year	**(86,277)**	(83,606)	**(86,277)**	(83,606)
Foreign exchange gain/(loss) on revaluation	**172,250**	(96,500)	**172,250**	(96,500)
Amortisation of deferred income on Government grant – CBSL Swap	**85,973**	(180,106)	**85,973**	(180,106)
Fair value at 31 December	**654,583**	701,665	**654,583**	701,665

DFCC Bank PLC in October 2013 raised USD 100 million by Issue of Notes abroad repayable in October 2018. The proceeds of this note issue are to be deployed predominantly in LKR denominated monetary assets. In order to hedge the resulting net open foreign currency liability position, DFCC Bank PLC has entered into a annualy renewable currency SWAP arrangement with Central Bank of Sri Lanka (CBSL) for 75% of the US Dollar (USD) denominated liability. Accordingly this contract was renewed in November 2016.

The currency SWAP arrangement, pursuant to Government policy for the principal amount only is designed to reimburse DFCC Bank by CBSL for any exchange loss incurred and conversely for DFCC Bank to pay CBSL any exchange gain arising from depreciation of LKR *vis-a-vis* USD or appreciation of LKR *vis-a-vis* USD respectively.

Although, USD denominated notes are repayable at the end of 5 years, the currency SWAP arrangement contract is renewed annually up to the date of repayment of the notes so as to exchange cash flow arising from movement in USD/LKR spot exchange rate that occurs at the time of renewal of the annual contract.

The currency SWAP arrangement with CBSL provides for SWAP of LKR to USD at the end of the contract at the same spot rate as the initial SWAP of USD to LKR at the commencement of the annual contract. (i.e. CBSL SWAP arrangement amounts to a full discount to USD LKR spot rate at the end of the contract.)

The hedging instrument for currency swap is deemed to be a derivative asset recognised at the fair value at the inception of the contract.

The fair value of this derivative asset is measured by reference to forward exchange quotes for USD purchase contracts by commercial banks, who are the normal market participants. Thus the fair value gain at the inception of the contract is the full amount of the forward premium quote at the end of one year.

The subsequent change in fair value is recognised in the income statement.

CBSL normally does not enter into forward exchange contracts with market participants providing 100% discount to the USD LKR spot rate at the time of the maturity of the contract. Thus this arrangement has features of both derivative instrument and Government grant through the agency of CBSL.

The initial gain by reference to forward price of an equivalent forward exchange dollar purchase contract is recognised as a Government grant and deferred income.

The deferred income is amortised on a systematic basis over the period in which the Bank recognises the fall in value of derivative which the grant is intended to compensate.

	BANK		GROUP	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000

42 Deferred Tax Asset/Liability

Deferred tax liability (Note 42.1)	**1,194,027**	851,662	**1,232,478**	873,912
Deferred tax asset (Note 42.2)	**–**	–	**3,160**	628
Net total	**1,194,027**	851,662	**1,229,318**	873,284

42.1 Deferred Tax Liability

Balance at beginning	**991,492**	1,021,744	**1,013,742**	1,022,192
Recognised in income statement	**87,393**	(30,252)	**103,594**	(8,002)
Recognised in other comprehensive income	**190,583**	–	**190,583**	(448)
	1,269,468	991,492	**1,307,919**	1,013,742
Transferred from deferred tax asset	**(75,441)**	(139,830)	**(75,441)**	(139,830)
Balance as at 31 December	**1,194,027**	851,662	**1,232,478**	873,912

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

42.2 Deferred Tax Asset

Balance at beginning	**139,830**	141,254	**140,458**	143,238
Recognised in income statement	**10,973**	(69,953)	**14,048**	(70,623)
Recognised in other comprehensive income	**(75,362)**	68,529	**(75,905)**	67,843
	75,441	139,830	**78,601**	140,458
Offset against deferred tax liability	**(75,441)**	(139,830)	**(75,441)**	(139,830)
Balance as at 31 December	–	–	**3,160**	628

42.3 Recognised Deferred Tax Assets and Liabilities

Assets				
Property, equipment and software	–	–	**(898)**	(1,234)
Gratuity liability and actuarial losses on defined benefit plans	**75,441**	61,868	**79,499**	63,730
Fair value of available-for-sale financial assets	–	77,962	–	77,962
	75,441	139,830	**78,601**	140,458
Liabilities				
Property, equipment and software	**176,168**	133,762	**200,418**	156,012
Finance leases	**902,717**	857,730	**902,717**	857,730
Fair value of available-for-sale financial assets	**190,583**	–	**190,583**	–
Undistributed profits of the group	–	–	**14,201**	–
	1,269,468	991,492	**1,307,919**	1,013,742

42.3.1 Tax on Gains on Disposal

With the introduction of new Inland Revenue Act No. 24 of 2017 the business assets/capital assets will attract tax at the corporate tax rate on the gains at the time of disposal. Accordingly deferred tax liability is expected to be provided for free hold land. However as the Bank/Group is under cost model, no deferred tax liability has been provided in these Financial Statements.

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

42.4 Unrecognised Deferred Tax Assets

Accumulated tax losses				
DFCC Consulting (Pvt) Limited – Subsidiary	–	–	**5,956**	6,114
Synapsys Limited – Subsidiary	–	–	**6,972**	7,321
	–	–	**12,928**	13,435

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

43 Other Assets

Refundable deposits and advances	**370,300**	323,819	**372,070**	330,694
Debtors	**805,204**	720,796	**834,334**	760,598
Clearing account balances	**1,600,238**	1,521,021	**1,600,238**	1,521,021
Receivable from pension fund	**181,820**	165,363	**181,820**	165,363
	2,957,562	2,730,999	**2,988,462**	2,777,676

44 Due to Banks

Balances with foreign banks	**1,067,474**	1,536,573	**1,067,474**	1,536,573
Borrowing – local banks	**8,573,261**	12,063,868	**8,573,261**	12,063,868
Securities sold under repurchase (Repo) agreements	**–**	4,503,146	**–**	4,503,146
	9,640,735	18,103,587	**9,640,735**	18,103,587

45 Due to Other Customers

Total amount due to other customers	**193,307,534**	140,514,373	**192,920,147**	140,219,872

45.1 Analysis

45.1.1 By Product

Demand deposits (current accounts)	**4,468,869**	4,649,369	**4,468,192**	4,648,714
Savings deposits	**36,660,313**	23,798,492	**36,657,366**	23,776,214
Fixed deposits	**151,284,299**	111,052,817	**150,900,536**	110,781,249
Certificate of deposits	**477,711**	739,483	**477,711**	739,483
Other deposits	**416,342**	274,212	**416,342**	274,212
	193,307,534	140,514,373	**192,920,147**	140,219,872

45.1.2 By Currency

Sri Lanka Rupee	**151,552,198**	112,168,697	**151,172,107**	111,881,136
United States Dollar (USD)	**37,950,742**	23,790,651	**37,943,446**	23,783,711
Great Britain Pound (GBP)	**1,044,429**	1,521,875	**1,044,429**	1,521,875
Others	**2,760,165**	3,033,150	**2,760,165**	3,033,150
	193,307,534	140,514,373	**192,920,147**	140,219,872

46 Other Borrowing

Repayable in foreign currency				
Borrowing sourced from				
Multilateral institutions	**3,281,998**	3,820,210	**3,281,998**	3,820,210
Bilateral institutions	**11,266,708**	3,995,545	**11,266,708**	3,995,545
	14,548,706	7,815,755	**14,548,706**	7,815,755

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Repayable in Rupees				
Borrowing sourced from				
Multilateral Institutions	**19,395,507**	18,536,211	**19,395,507**	18,536,211
Bilateral Institutions	**1,369,093**	1,154,259	**1,369,093**	1,154,259
Central Bank of Sri Lanka – refinance loans (secured)	**199,625**	250,548	**199,625**	250,548
Securities sold under repurchase (Repo) agreements	**5,806,660**	12,994,573	**5,777,943**	12,979,527
	26,770,885	32,935,591	**26,742,168**	32,920,545
	41,319,591	40,751,346	**41,290,874**	40,736,300

46.1 Assets Pledged as Security

Nature	**Amount 31.12.2017 LKR 000**
Assignment in terms of Section 88 A of the Monetary Law of Loans refinanced by Central Bank	**199,625**

47 Debt Securities Issued

Year of Issuance	Face value LKR 000	Interest rate %	Repayment terms	Issue date	Maturity date	BANK/GROUP 31.12.2017 LKR 000	BANK/GROUP 31.12.2016 LKR 000
Issued by Bank							
i. Debenture issue (LKR)							
– Listed	–	8.36	3 Years	18 Aug. 14	18 Aug. 17	–	5,138,232
	3,000,000	9.10	5 Years	10 Jun. 15	10 Jun. 20	**3,136,708**	3,131,330
	5,315,450	10.63	3 Years	18 Mar. 16	18 Mar. 19	**5,747,779**	5,745,558
ii. Notes issue (USD)	15,360,000	9.63	5 Years	31 Oct. 13	31 Oct. 18	**15,559,280**	15,164,065
	23,675,450					**24,443,767**	29,179,185
Due within one year						**15,559,280**	5,138,232
Due after one year						**8,884,487**	24,040,953
						24,443,767	29,179,185

Carrying values are the discounted amounts of principal and interest.

47.1 Debt Securities Issued – Listed Debentures

Debenture category	Interest payable frequency	Applicable interest rate %	Interest rate of Comparative Government securites (Gross) p.a. %	Balance as at 31-12-2017 LKR 000	Market price Highest	Market price Lowest	Market price Last traded	Yield last traded %
Fixed Rate								
2015-2020	Annually	9.1	9.62	**3,136,708**	N/T	N/T	N/T	N/A
2016-2019	Annually	10.63	9.29	**5,747,779**	N/T	N/T	N/T	N/A

Other Ratios	**31.12.2017**	31.12.2016
Debt to equity Ratio	**1.77**	2.12
Interest cover	**0.99**	1.01
Liquid asset ratio (%)	**26.8**	27.2

As at	BANK **31.12.2017 LKR 000**	BANK 31.12.2016 LKR 000	GROUP **31.12.2017 LKR 000**	GROUP 31.12.2016 LKR 000

48 Other Liabilities

Accruals	**416,079**	395,545	**420,742**	412,010
Prior year's dividends	**47,318**	57,538	**47,318**	57,538
Security deposit for leases	**4,065**	4,065	**81,544**	44,888
Prepaid loan and lease rentals	**56,836**	57,166	**108,980**	84,442
Account payables	**3,086,110**	2,925,313	**3,120,922**	2,978,449
Provision for staff retirement benefits (Note 48.1)	**330,578**	282,684	**352,710**	306,640
Other provisions (Note 48.2)	**525,412**	468,364	**525,412**	468,364
	4,466,398	4,190,675	**4,657,628**	4,352,331

48.1 Provision for Staff Retirement Benefits

Defined benefit – unfunded pension (Note 48.1.1)	**61,147**	61,728	**61,147**	61,728
– unfunded end of service gratuity (Note 48.1.2)	**269,431**	220,956	**291,563**	244,912
– funded pension (Note 48.1.3)				
	330,578	282,684	**352,710**	306,640

As at	BANK/GROUP **2017 LKR 000**	BANK/GROUP 2016 LKR 000

48.1.1 Unfunded Pension Liability

Balance at beginning	**61,728**	66,994
Interest on obligation	**5,794**	5,688
Benefits paid	**(6,995)**	(6,995)
Actuarial experience loss	**620**	608
Actuarial gain due to changes in assumptions	–	(4,567)
Present value of defined benefit pension obligations	**61,147**	61,728

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

48.1.2 Unfunded End of Service Gratuity

Balance at beginning	**220,956**	180,163	**244,812**	206,016
Liability transferred	**2,414**	3,416	–	–
Current Service cost	**35,041**	29,417	**41,507**	33,853
Interest on obligation	**22,096**	17,440	**23,877**	19,218
Benefits paid	**(20,363)**	(20,488)	**(24,652)**	(22,396)
Actuarial experience loss	**9,287**	11,306	**6,019**	8,519
Actuarial gain due to changes in assumptions	–	(298)	–	(298)
Present value of defined benefit pension obligations	**269,431**	220,956	**291,563**	244,812

As at	BANK/GROUP 2017 LKR 000	BANK/GROUP 2016 LKR 000

48.1.3 Funded Pension Liability/(Asset)

Present value of defined benefit pension obligations (Note 48.1.3.1)	**2,372,248**	2,280,943
Fair value of pension assets (Note 48.1.3.2)	**(2,554,068)**	(2,446,306)
Defined benefit liability/(asset)	**(181,820)**	(165,363)

As per LKAS 19 – "Employee Benefits" if a plan is in surplus, then the amount recognised as an asset in the Statement of Financial Position is limited to the "asset ceiling". The asset ceiling is the present value of any economic benefits available to the entity in the form of a refund or a reduction in future contributions. By analysing all the future economic benefits available to the DFCC Pension Fund, the independent actuary Mr Piyal S Goonetilleke of Priyal S Goonetilleke & Associate has estimated the asset ceiling as at 31 December 2017 to be LKR 287 million in his report dated 13 February 2017.

As at	BANK/GROUP 2017 LKR 000	BANK/GROUP 2016 LKR 000

48.1.3.1 Movement in Defined Pension Obligation

Present value of defined benefit pension obligations at the beginning	**2,280,943**	2,296,454
Current service cost	**60,496**	71,746
Interest on obligation	**228,094**	206,681
Benefits paid	**(197,770)**	(155,931)
Actuarial experience loss	**485**	85,266
Actuarial gain due to changes in assumptions	–	(223,273)
Present value of defined benefit pension obligations	**2,372,248**	2,280,943

As at	BANK/GROUP 2017 LKR 000	BANK/GROUP 2016 LKR 000

48.1.3.2 Movement in Pension Assets

	2017 LKR 000	2016 LKR 000
Pension assets at the beginning	**2,446,306**	2,237,646
Expected return on pension assets	**233,917**	193,785
Employer's contribution	**28,823**	164,000
Benefits paid	**(197,770)**	(155,931)
Actuarial experience gain	**42,792**	6,806
Pension assets	**2,554,068**	2,446,306

48.1.3.3 Plan Assets Consist of the following

	2017 LKR 000	2016 LKR 000
Debentures	**119,184**	216,555
Government bonds	**231,899**	1,439,581
Fixed deposits	**2,211,589**	789,623
Others	**(190,424)**	547
	2,372,248	2,446,306

As at	Unfunded pension liability* 31.12.2017 LKR 000	Unfunded end of service gratuity* 31.12.2017 LKR 000	Funded pension liability* 31.12.2017 LKR 000

48.1.3.4. The Expected Benefit Payout in the Future Years to the Defined Benefit Obligation – Bank

	Unfunded pension liability* 31.12.2017 LKR 000	Unfunded end of service gratuity* 31.12.2017 LKR 000	Funded pension liability* 31.12.2017 LKR 000
Within next 12 months	**6,995**	**21,390**	**165,455**
Between 2 and 5 years	**27,982**	**143,510**	**784,418**
Beyond 5 years	**34,977**	**338,501**	**1,460,791**

** Based on expected benefits payout in next 10 years*

48.1.3.5 Unfunded Pension Liability

This relates to pension liability of an ex-employee, not funded through the DFCC Bank PLC Pension Fund. The liability covers the pension benefit to retiree and survivors.

48.1.3.6 Actuarial Valuation

Actuarial valuation was carried out by Mr Piyal S Goonetilleke, Fellow of the Society of Actuaries USA of Priyal S Goonetilleke & Associates, on 31 December 2017.

48.1.3.7 Actuarial Valuation Method

Projected unit credit method was used to allocate the actuarial present value of the projected benefits earned by employees to date of valuation.

	31 December 2017		31 December 2016	
	Pension benefit (%)	**End of service gratuity (%)**	Pension benefit (%)	End of service gratuity (%)
48.1.3.8 Principal Actuarial Assumptions				
Discount rate per annum				
Pre-retirement	**10**	**10**	10	10
Post-retirement	**10**	**Not applicable**	10	Not applicable
Future salary increases per annum	**10.5**	**10.5**	10.5	10.5
Expected rate of return on pension assets	**10**	**–**	10	–
Actual rate of return on pension assets	**11.8**	**–**	11.8	–
Mortality	**UP 1984 mortality table**	**RP-2000 mortality table**	UP 1984 mortality table	RP-2000 mortality table
Retirement age	**55 years**	**55 years**	55 years	55 years
Normal form of payment:	**Lump sum commuted pension payment followed by reduced pension for 10 years (25% reduction) (for new entrants recovery period is 15 years)**	**Lump sum**	Lump sum commuted pension payment followed by reduced pension for 10 years (25% reduction) (for new entrants recovery period is 15 years)	Lump sum
Turnover rate –				
Age				
20	**10.0**	**10.0**	10.0	10.0
25	**10.0**	**10.0**	10.0	10.0
30	**10.0**	**10.0**	10.0	10.0
35	**7.5**	**7.5**	7.5	7.5
40	**5.0**	**5.0**	5.0	5.0
45	**2.5**	**2.5**	2.5	2.5
50/55	**1.0**	**1.0**	1.0	1.0

The principle actuarial assumptions in the previous year has not changed. The discount rate is the yield rate on 31 December 2017 with a term equalling the estimated period for which all benefit payments will continue. This period is approximately 22.4 years for pension and 10.6 years for end of service gratuity.

48.1.3.9 Principal Actuarial Assumptions – Group

The subsidiaries have used discount rate of 10.5% and the salary increment rate ranging 6.6% – 8%.

48.1.3.10 Sensitivity of Assumptions Used in the Actuarial Valuation

The following table demonstrates the sensitivity to a reasonably possible change in the key assumptions used with all other variables held constant in the employment benefit liability measurement. The effect in the income statement and the statement of financial position with the assumed changes in the discount rates and salary increment rate is given below:

	Effect on income statement increase/(decrease) LKR 000	Effect on defined benefit obligation increase/(decrease) LKR 000
Funded Pension Liability		
Discount rate		
1%	94,927	(94,927)
-1%	(227,378)	227,378
Salary increment rate		
1%	(44,561)	44,561
-1%	42,054	(42,054)
Unfunded Pension Liability		
Discount rate		
1%	3,920	(3,920)
-1%	(4,446)	4,446
Unfunded End of Service Gratuity *		
Discount Rate		
1%	27,870	(27,870)
-1%	(32,816)	32,816
Salary increment rate		
1%		
-1%	(31,626)	31,626
	27,439	(27,439)

** Salary increment not applicable for ex-employee*

48.1.3.11 Historical Information

As at	31.12.2016 LKR 000	31.12.2015 LKR 000	31.03.2015 LKR 000	31.03.2014 LKR 000	31.03.2013 LKR 000
Present value of the defined benefit obligation	2,280,943	2,296,454	2,141,648	1,866,434	1,750,987
Fair value of plan assets	(2,446,306)	(2,237,646)	2,139,052	2,027,664	1,821,009
(Surplus)/Deficit in the plan	(165,363)	58,808	2,596	(161,230)	(70,022)

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000

48.2 Other Provisions

Balance as at the beginning	**468,364**	414,702	**468,364**	414,702
Provisions for the financial year	**525,412**	468,364	**525,412**	468,364
Provisions used during the year	**(452,256)**	(401,927)	**(452,256)**	(401,927)
Provisions reversed during the year	**(16,108)**	(12,775)	**(16,108)**	(12,775)
Balance as at 31 December	**525,412**	468,364	**525,412**	468,364

49 Subordinated Term Debt

	Face value LKR 000	Interest rate %	Repayment terms	Issue date	Maturity date	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Listed Debentures									
Issued by Bank	6,043,140	12.75	7 years	9-Nov-16	9-Nov-23	**6,129,480**	6,131,261	**6,129,480**	6,131,261
	956,860	12.15	5 years	9-Nov-16	9-Nov-21	**970,023**	970,094	**970,023**	970,094
Transferred on amalgamation	2,000,000	9.4	5 years	10-Jun-15	10-Jun-20	**2,103,367**	2,104,282	**2,103,367**	2,104,282
	9,000,000					**9,202,870**	9,205,637	**9,202,870**	9,205,637
Due after one year						**9,202,870**	9,205,637	**9,202,870**	9,205,637
						9,202,870	9,205,637	**9,202,870**	9,205,637

49.1 Subordinated Term Debt – Listed Debentures

Debenture category	Interest rate frequency %	Applicable interest rate	Interest rate of comparative government securities (Gross) p.a %	Balance as at 31.12.2017 LKR 000	Market price Highest	Market price Lowest	Market price Last traded	Yield last traded %
Fixed Rate								
2015-2020	Annually	9.4	9.62	**2,103,367**	N/T	N/T	N/T	N/A
2016-2021	Annually	12.15	9.75	**970,023**	N/T	N/T	N/T	N/A
2016-2023	Annually	12.75	10.01	**6,129,480**	100.5	100	100	12.71
				9,202,870				

N/T – Not traded
Debt equity ratio, interest cover and liquid asset ratio is given in note 47.1.

As at	BANK/GROUP 31.12.2017 LKR 000	BANK/GROUP 31.12.2016 LKR 000

50 Stated Capital

Balance as at 31 December (Number of shares – 265,097,688)	**4,715,814**	4,715,814

51 Statutory Reserves

51.1 Reserve Fund

Five per cent of profit after tax is transferred to the reserve fund as per Direction issued by Central Bank of Sri Lanka under Section 76 (j) (1) of the Banking Act No. 30 of 1988 as amended by Banking (Amendment) Act No. 33 of 1995.

52 Retained Earnings

This represents cumulative net earnings, inclusive of final dividend approved amounting to LKR 1,325 million. The balance is retained and reinvested in the business of the bank.

	BANK		GROUP	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000
53 Other Reserves				
General reserve	**13,779,839**	13,779,839	**13,779,839**	13,779,839
Fair value reserve	**13,298,686**	14,549,487	**11,032,483**	12,085,454
Exchange equalisation reserve	**–**	–	**13,061**	33,428
	27,078,525	28,329,326	**24,825,383**	25,898,721

54 Commitments and Contingencies

Accounting Policy →

Commitments and Contingencies

Contingent liabilities, which include guarantees are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of the Bank; or are present obligations that have arisen from past events but are not recognised because it is not probable that settlement will require the outflow of economic benefits, or because the amount of the obligations cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

Financial Guarantees

Liabilities under financial guarantee contracts are recorded initially at their fair value, which is generally the fee received or receivable. Subsequently, financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure required to settle the obligations.

As at	BANK		GROUP	
	31.12.2017 LKR 000	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000

54.1 Commitments and Contingencies

Guarantees issued to –				
Banks in respect of indebtedness of customers of the Bank	**135,464**	34,403	**135,464**	34,403
Companies in respect of indebtedness of customers of the Bank	**9,297,340**	5,092,952	**9,297,340**	5,092,952
Principal collector of customs (duty guarantees)	**276,587**	313,295	**276,587**	313,295
Shipping guarantees	**2,939,459**	1,541,757	**2,939,459**	1,541,757
Documentary credit	**15,098,107**	9,763,476	**15,098,107**	9,763,476
Bills for collection	**2,305,466**	3,148,059	**2,305,466**	3,148,059
Performance bonds	**3,922,424**	2,461,709	**3,922,424**	2,461,709
Forward exchange contracts (net)	**38,118,013**	26,704,132	**38,118,013**	26,704,132
Commitments in ordinary course of business – Commitments for unutilised credit facilities	**62,852,575**	52,059,192	**62,852,575**	52,059,192
Capital expenditure approved by the Board of Directors				
Contracted	**288,635**	202,692	**288,635**	202,692
Not contracted	**337,254**	130,434	**337,254**	130,434
	135,571,324	101,452,101	**135,571,324**	101,452,101

54.2 Litigation Against the Bank

54.2.1 A client has filed action against five defendants including the Bank in the District Court of Kurunegala, claiming that a property mortgaged by him to the Bank had been unlawfully transferred to a third party under the parate process to be set aside, and also claiming LKR 6 million as damages from the Bank. The Bank is defending the case before the District Court.

54.2.2 There are four cases filed in the District Court of Kandy and one case filed in the District Court of Negombo and another case in the District Court of Moratuwa, where third parties are claiming ownership of properties acquired by the Bank under recovery action. The Bank is defending the cases before the respective District Courts.

54.2.3 There is one cases filed in the District Court of Bandarawela, where a third party is claiming ownership of a property mortgaged to the Bank. The Bank is defending the cases before the respective District Court.

54.2.4 There are two cases filed in the District Court of Anuradhapura, by a customer claiming damages due to a cancellation by the insurer of an insurance policy covering a mortgaged asset and claiming damages for not insuring a mortgaged asset. The Bank is defending the cases before the District Court.

54.2.5 There is one case filed in the District Court of Theldeniya, where a third party is claiming ownership of a property mortgaged to the Bank. The Bank is defending the case before the District Court of Theldeniya.

54.2.6 A client has filed a case in the District Court of Matara claiming damages from the Bank claiming that as the loan was not disbursed in lump sum but in instalments bases on the client's progress as such his business went into decline and he suffered losses. The Bank is defending the case before the District Court of Matara.

54.2.7 The Bank has appealed to the High Court to set aside an award made in favour of an ex-employee by the Labour Tribunal.

54.2.8 Case filed in the Labour Tribunal by one ex-employee of the Bank, claiming compensation from the Bank.

54.2.9 Case filed in the Labour Tribunal – Galle by an ex-employee of the Bank, claiming compensation and reinstatement from the Bank.

No material losses are anticipated as a result of the aforesaid actions.

54.3 Tax Assessments Against the Bank

The following assessments are outstanding, against which the Bank has duly appealed.

1. The income tax assessment received by the Bank for the Year of Assessment 2010/11, which was determined by the Commissioner General of Inland Revenue amounting to LKR 760 million has been appealed to the Tax Appeal Commission for their determination.
2. Tax assessments received by the Bank on Value Added Tax for quarters ending 31.03.2016, 30.06.2016 and 30.09.2016, charging a penalty of LKR 2.8 million, due to differences in records of the Department of Inland Revenue. The bank has paid all the taxes on due dates and accordingly has appealed against these assessments.

The Bank is of the view that the above assessments will not have any significant impact on the financial statements.

55 Related Party Transactions

55.1 The Group's related parties include associates, subsidiaries, Trust established by the Bank for post-employment retirement plan, joint venture, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced for which significant voting power is held by Key Management Personnel or their close family members.

55.2 Parent and Ultimate Controlling Party

The Bank does not have an identifiable parent of its own.

As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000
55.3 Transactions with Subsidiaries		
55.3.1 Statement of Financial Position – Bank		
Liabilities		
Due to other customers	**380,431**	290,777
Other borrowings	**28,058**	15,065
	408,489	305,842

Year ended 31 December	**2017 LKR 000**	2016 LKR 000
55.3.2 Income Statement – Bank		
Interest income	**23**	20
Interest expense	**45,710**	29,930
Fee and commission income	**33**	44
Other operating income (net)	**413**	317
Net gain from financial investments – dividend received	**51,466**	44,596
Other overhead expenses net of reimbursements	**106,067**	125,412
55.3.3 Other Transactions – Bank		
Payments made for purchase of computer software	**43,782**	31,134

As at	31.12.2017 LKR 000	31.12.2016 LKR 000

55.4 Transactions with Joint Venture

55.4.1 Statement of Financial Position – Bank

Assets		
Loans to and receivable from other customers	**127,522**	146,271
	127,522	146,271
Liabilities		
Due to other customers	**442**	1,506
Debt securities issued	**–**	103
	442	1,609

Year ended 31 December	2017 LKR 000	2016 LKR 000

55.4.2 Income Statement – Bank

Interest income	**18,258**	–
Interest expenses	**–**	8
Fee and commission income	**1**	–
Net Gain from financial investments – dividend received	**33,220**	30,200

As at	31.12.2017 LKR 000	31.12.2016 LKR 000

55.5 Transactions with Associate

55.5.1 Statement of Financial Position-Bank

Liabilities		
Due to other customers	**306**	135
	306	135

Year ended 31 December	2017 LKR 000	2016 LKR 000

55.5.2 Income Statement – Bank

Fee and commission income	**15**	–
Net gain from financial investments – dividend received	**6,777**	9,463

As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000

55.6 Transaction with Entities in which Directors of the Bank have Significant Influence

55.6.1 Statement of Financial Position – Bank

Assets		
Loans to and receivables from other customers	**63,803**	–
	63,803	–
Liabilities		
Due to other Customers	**1,158**	–
	1,158	–

Year ended 31 December	**2017 LKR 000**	2016 LKR 000

55.6.2 Income Statement – Bank

Interest income	**250**	–
Interest expenses	**11**	–
Fee and commission income	**973**	–
Other overhead expense	**30**	–

55.7 Transactions with Key Management Personnel

55.7.1 Key Management Personnel

Key Management Personnel are the Board of Directors of the Bank including Chief Executive, Deputy Chief Executive, Executive Vice President Strategic Planning and Subsidiaries, Chief Risk Officer, Chief Financial Officer, Chief Operating Officer, and Senior Vice President Treasury and Resource Mobilisation for the purpose of Sri Lanka Accounting Standard – LKAS 24 on "Related Party Disclosures".

	BANK		GROUP	
	Year ended 31.12.2017 LKR 000	Year ended 31.12.2016 LKR 000	**Year ended 31.12.2017 LKR 000**	Year ended 31.12.2016 LKR 000

55.7.2 Compensation of Directors and Other Key Management Personnel

Number of persons	**14**	16	**16**	18
Short-term employment benefits	**139,434**	124,920	**155,950**	139,575
Post-employment benefits – Pension	**1,931**	2,494	**1,931**	2,494
– Others	**17,528**	15,115	**17,983**	15,524
	158,893	142,529	**175,864**	157,593

As at	31.12.2017		31.12.2016	
	Number of KMPs	**LKR 000**	Number of KMPs	LKR 000

55.7.3 Other Transactions with Key Management Personnel and their Close Family Members

55.7.3.1 Statement of Financial Position – Bank

Assets				
Loans to and receivables from other customers	**4**	**22,994**	6	17,289
Liabilities				
Due to other customers	**18**	**270,569**	21	285,106
Other borrowings	**1**	**32,489**	1	16,400
Debt securities issued	**1**	**2,168**	1	2,168
		305,226		303,674

	Year ended 31.12.2017 LKR 000	Year ended 31.12.2016 LKR 000

55.7.3.2 Income Statement – Bank

Interest income	**1,265**	877
Interest expense	**30,575**	20,405
Fee and commission income	**5**	5

55.7.4 Accommodation Granted to Directors of the Bank

Disclosure under Section 47 (11A) of the Banking Act, No. 30 of 1988 as amended by Amendment Act No. 2 of 2005

Name of Director	Limit LKR 000	Type of Facility	**Balance as at 31.12.2017 LKR 000**
C R Jansz	500	Credit Card	–
L H A L Silva	500	Credit Card	–
S R Thambiayah	500	Credit Card	–
			–

55.7.5 Transactions with DFCC Bank Pension Fund – Trust

DFCC Bank Pension Fund constituted as a Trust was established by the DFCC Bank to discharge defined benefit pension liability of eligible employees of the Bank.

	31.12.2017 LKR 000	31.12.2016 LKR 000
Contribution prepaid/(payable) as at beginning	**165,363**	(58,808)
Contribution due for the financial year recognised as expense in income statement	**(54,673)**	(84,642)
Recognition of actuarial gains in the other comprehensive income	**42,307**	144,813
Contribution paid by the Bank	**28,823**	164,000
Contribution prepaid (Note 48.1.3)	**181,820**	165,363

55.8 Transactions with Government of Sri Lanka (GOSL) and its Related Entities

Entities related to the Government of Sri Lanka (GOSL) by virtue of their aggregate shareholdings has the power to participate in the financial and operating policy decision of the Bank and by extension to participate in the financial and operating policy decisions of the Bank. However, in fact this power was not exercised.

Paragraph 25 of Sri Lanka Accounting Standard Related Party Disclosure – LKAS 24 has exempted DFCC Bank from the normally applicable disclosure requirements on transactions with GOSL – related entities. In making use of this exemption the Board has determined that the limited disclosure required under paragraph 26 of LKAS 24 is only required to be made for transaction that are individually significant because of their size although these transactions were undertaken on normal market terms in the ordinary course of business and there was no requirement to disclose the transactions to regulatory or supervisory authorities or require shareholder approval.

55.8.1 Individually Significant Transactions Included in the Statement of Financial Position

As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000
55.8.1.1 Statement of Financial Position – Bank		
Assets		
Balances with Central Bank of Sri Lanka	**10,557,688**	8,062,567
Placements with banks	**100,060**	–
Loans to and receivables from banks	**10,956,289**	12,213,311
Loans to and receivables from other customers	**7,130,529**	5,859,992
Other financial assets held for trading	**279,094**	–
Financial investments – held to maturity	**18,376,228**	17,239,338
Financial investments available for sale	**37,746,039**	29,365,255
Government grant receivable	**642,582**	861,914
	85,788,509	73,602,377
Liabilities		
Due to Banks	**7,315,012**	7,672,071
Due to other customers	**3,952,692**	5,796,290
Other borrowing	–	8,388,916
Other borrowing – credit lines	**23,351,882**	23,761,357
Debt securities issued	**2,138,927**	2,393,335
Government grant deferred income	**654,582**	701,664
Subordinated term debt	**3,528,506**	3,004,003
	40,941,601	51,717,636
Commitments		
Undrawn credit facilities	**8,740,754**	3,494,485

	Year ended 31.12.2017 LKR 000	Year ended 31.12.2016 LKR 000
55.8.1.2 Income Statement – Bank		
Interest income	**6,418,084**	3,454,367
Net gain/(loss) from trading	**2,231**	(9,880)
Interest expense	**3,156,669**	3,050,930

There are no other transactions that are collectively significant with Government-related entities.

55.9 Disclosure Requirement under Section 9.3.2 (a) and 9.3.2 (b) of the CSE Listing Rules

As per rule No. 9.3.2 (a) the Bank does not have any non-recurrent related party transactions carried out during the financial year under review with a value exceeding 10% of the equity or 5% of the total assets whichever is lower, as per the audited financial statements of the Bank.

As per rule No. 9.3.2 (b) the Bank has following recurrent related party transactions carried out during the financial year under review with value exceeding 10% of the gross revenue/income as per the latest audited financial statements of the bank.

Name of the related party	Relationship	Nature of the transaction	Aggregate value of related party transactions entered into during the financial year	Aggregate value of related party transactions as a % of net revenue/income	Terms and conditions of the related party transactions
Entities related to the Government of Sri Lanka	Related party	On Balance Sheet and off Balance Sheet credit facility	Facilities approved during the year LKR 6,691.5 million	0.83%*	Terms and conditions under normal commercial terms similar to other non-related customers

**Actual income on the facilities disbursed and the projected annual income on the facilities offered not disbursed as a percentage of the total annual consolidated income of the Bank.*

55.10 Pricing Policy and Terms for Transactions with Related Parties

Bank enters into transactions with related parties in the ordinary course of business on terms similar to comparable transactions with an unrelated comparable counterparty with the exception of accommodation granted to Key Management Personnel under approved schemes uniformly applicable to all or specific categories of employees. The terms include pricing for loans, deposits and services, collateral obtained for loans where appropriate.

56 Business Segment Information

Business segment results include items directly attributable to a business segment as well as those that can be allocated on a reasonable basis. Unallocated items include corporate assets, head office expenses and tax assets and liabilities.

For the period ended 31 December 2017	Banking LKR 000	Finance leasing LKR 000	Investing in equity LKR 000	Other LKR 000	Unallocated LKR 000	Eliminations LKR 000	Total LKR 000
Group							
Revenue							
Interest income	30,912,425	2,074,165	–	54,654	–	(46,608)	32,994,636
Net fee and commission income	1,591,336	–	–	607	–	–	1,591,943
Net gain from trading	361,647	–	–	–	–	–	361,647
Net loss from financial instruments at fair value through profit or loss	(404,586)	–	–	–	–	–	(404,586)
Net gain from financial investments	197,915	–	2,040,251	–	–	(293,048)	1,945,118
Other operating (loss)/income – net	(831,541)	–	–	497,772	–	(167,898)	(501,667)
Total income	31,827,196	2,074,165	2,040,251	553,033	–	(507,554)	35,987,091
Percentage*	88	6	5	2	–	(1)	100

For the period ended 31 December 2017	Banking LKR 000	Finance leasing LKR 000	Investing in equity LKR 000	Other LKR 000	Unallocated LKR 000	Eliminations LKR 000	Total LKR 000
Expenses							
Segment losses	1,121,003	32,598	22,811	3,850	–	(9,896)	1,170,366
Depreciation	–	–	–	41,836	–	–	41,836
Other operating and interest expense	24,782,926	1,591,944	–	326,677	–	(231,054)	26,470,493
	25,903,929	1,624,542	22,811	372,363	–	(240,950)	27,682,695
Result	5,923,267	449,623	2,017,440	180,670	–	(266,604)	8,304,396
Unallocated expenses							1,139,267
Value added tax and nation building tax on financial services							1,458,749
Operating profit after value added tax and nation building tax on financial services							5,706,380
Share of profits of associate and joint venture							185,030
Profit before income tax							5,891,410
Income tax expense							1,457,653
Profit for the year							4,433,757
Other comprehensive expenses net of tax							(1,032,435)
Total comprehensive income							3,401,322
Total comprehensive income – non-controlling interests							71,572
Profit attributable to equity holders of the Bank							3,329,750
Assets	269,505,984	16,493,374	19,201,495	915,651	27,271,249	(603,868)	332,783,885
Percentage*	81	5	6	–	8	–	100
Investments in associate and joint venture company							1,683,977
Liabilities	242,555,385	14,844,037	–	258,360	27,845,355	(437,132)	285,066,005
Capital expenditure – additions	–	–	–	10,015	605,297	–	615,312

* *Net of eliminations.*

For the period ended 31 December 2016	Banking LKR 000	Finance leasing LKR 000	Investing in equity LKR 000	Other LKR 000	Unallocated LKR 000	Eliminations LKR 000	Total LKR 000
Group							
Revenue							
Interest income	22,360,944	1,833,214	–	42,070	–	(30,116)	24,206,112
Net fee and commission income	1,309,049	–	–		–		1,309,049
Net gain from trading	340,456	–	–	–	–	–	340,456
Net loss from financial instruments at fair value through profit or loss	(179,727)	–	–	–	–	–	(179,727)
Net gain from financial investments	152,695	–	1,012,694	–	–	(84,260)	1,081,129
Other operating (loss)/Income – net	(125,553)	–	–	469,396	50,123	(170,902)	223,064
Total income	23,857,864	1,833,214	1,012,694	511,466	50,123	(285,278)	26,980,083
Percentage*	88	7	4	2	–	(1)	100
Expenses							
Segment losses	882,415	–	54,852	–	–	(20,923)	916,344
Depreciation	–	–	–	38,254	–	–	38,254
Other operating and interest expense	18,399,506	1,300,127	–	310,902	–	(201,532)	19,809,003
	19,281,921	1,300,127	54,852	349,156	–	(222,455)	20,763,601
Result	4,575,943	533,087	957,842	162,310	50,123	(62,823)	6,216,482
Unallocated expenses							717,355
Value added tax and nation building tax on financial services							986,110
Operating profit after value added tax and nation building tax on financial services							4,513,017
Share of profits of associate and joint venture							161,151
Profit before income tax							4,674,168
Income tax expense							1,205,094
Profit for the year							3,469,074
Other comprehensive expenses net of tax							382,670
Total comprehensive income							3,851,744
Total comprehensive income – non-controlling interests							54,270
Profit attributable to equity holders of the Bank							3,797,474
Assets	236,081,685	15,909,152	20,018,918	790,936	17,416,817	(446,216)	289,771,292
Percentage*	81	5	7	1	6	–	100
Investments in associate and joint venture company							1,443,127
Liabilities	212,473,516	14,318,237	–	228,080	17,470,595	(334,584)	244,155,844
Capital expenditure – additions	–	–	–	39,942	218,550	–	258,492

* *Net of eliminations.*

56.1 Revenue and expenses attributable to the incorporated business segments of industrial estate management, information technology services and consultancy services are included in the column for other.

56.2 Property and equipment and depreciation attributable to an incorporated business segment is included in the relevant segment and the balance is unallocated.

56.3 Eliminations are the consolidation adjustments for inter-company transactions, dividend and dividend payable attributable to minority shareholders.

57 Comparative Figures

57.1 Reclassification of Comparative figures

The following information has been reclassified with the current year's classification in order to provide a better presentation.

	Current presentation		As disclosed previously	
	Bank LKR 000	Group LKR 000	Bank LKR 000	Group LKR 000
Prepayments	–	–	53,803	53,803
Other assets	2,730,999	2,777,676	2,728,340	2,775,017
Other borrowing	40,751,346	40,756,300	40,802,490	40,807,444

58 Events after the Reporting Period

58.1 First and Final Dividend

The Directors have approved the payment of a first and final dividend of LKR 5.00 per share for the year ended 31 December 2017. The Board of Directors confirms that the Bank has satisfied the solvency test in accordance with Section 57 of the Companies Act, No. 07 of 2007 and has obtained the certificate from the Auditors.

58.2 Proposed Debenture Issue

The Bank will issue fifty million (50,000,000) Basel III compliant, subordinated,listed, rated, unsecured, redeemable debentures with a non-viability conversion option, each at an issue price (par value) of LKR 100.00 with a term up to 7 years (“Debentures”), with an option to issue a further twenty million (20,000,000) of said Debentures in the event of an over subscription. After regulatory approvals, the resolution was taken up at the Extraordinary General Meeting held on 19 February 2018, and was approved by the shareholders.

No other circumstances have arisen which would require disclosure or adjustment to the financial statements.

59 Fair Value Measurement

59.1 Determining Fair Value

The determination of fair value for financial assets and financial liabilities, for which there is no observable market price, requires the use of valuation techniques as described in Note 5.3.5. For financial instruments that trade infrequently and have little price transparency, fair value is less objective and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. The Group's accounting policy on fair value measurements is discussed in Note 5.3.5. The Group measures fair values, using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.

Level 2: Valuation techniques based on observable inputs, either directly (i.e., prices) or indirectly (i.e., derived from prices).

This category includes instruments valued using quoted market prices in active markets for similar instruments, quoted prices for identical or similar instruments in markets that are considered less than active or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued, based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The Group uses widely recognised valuation models for determining the fair value of common and more simple financial instruments, like government securities, interest rate and currency swaps that use mostly observable market data and require little Management judgement and estimation. Observable prices and model inputs are usually available in the market for listed debt and equity securities, government securities and simple over the counter derivatives like forward exchange contracts and interest rate swaps. Availability of observable market prices and model inputs reduces the need for management judgement and estimation and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

Management judgements and estimations are usually required for selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instrument being valued, determination of probability of counterparty default and prepayments and selection of appropriate discount rates.

59.2 Valuation Framework

The established control framework with respect to the measurement of fair values, includes an oversight which is independent of front office management. Treasury Middle Office has overall responsibility for independently verifying the results of trading and investment operation.

Specific controls include:

- Verification of observable pricing
- Review and approval process for new models and changes to models involving both product control and group market risk
- Calibration and back testing of models
- Stress Testing

When third party information, such as broker quotes or pricing services is used to measure fair value, the evidence so obtained to support the conclusion that such valuations meet the requirements of SLFRSs/LKASs is documented.

This includes:

- Verifying that the broker or pricing service is approved by the Bank for use in pricing the relevant type of financial instrument
- Several quotes obtained from randomly selected brokers for the same financial instrument and the fair value determined on this basis

Any changes to the fair value methodology is reported to the Bank's Audit Committee.

59.3 Fair Value by Level of the Fair Value Hierarchy – Bank

As at 31 December 2017	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Total LKR 000
Financial Assets					
Derivative assets held-for-risk management	27				
Forward foreign exchange contracts		–	**66,440**	–	**66,440**
Other financial assets held for trading	28				
Government of Sri Lanka Treasury Bills and Bonds		**279,098**	–	–	**279,098**
Equity securities		**31,828**	–	–	**31,828**
Financial investments – Available for sale	31				
Government of Sri Lanka Treasury Bills and Bonds		**37,746,039**	–	–	**37,746,039**
Quoted ordinary shares		**18,195,008**	–	–	**18,195,008**
Units in Unit Trusts – Quoted		**194,590**	–	–	**194,590**
Units in Unit Trusts – Unquoted		–	**644,862**	–	**644,862**
Unquoted shares		–	–	**85,555**	**85,555**
Government grant receivable	41	–	**642,583**	–	**642,583**
		56,446,563	1,353,885	**85,555**	**57,886,003**
Financial Liabilities					
Derivative liabilities held-for-risk management	28				
Forward foreign exchange contracts		–	**367,435**	–	**367,435**
		–	**367,435**	–	**367,435**

As at 31 December 2016	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Total LKR 000
Financial Assets					
Derivative assets held-for-risk management	27				
Forward foreign exchange contracts		–	122,977	–	122,977
Financial investments – Available for sale	31				
Government of Sri Lanka Treasury Bills and Bonds		29,365,255	–	–	29,365,255
Quoted ordinary shares		18,797,640	–	–	18,797,639
Units in Unit Trusts – Quoted		190,153	–	–	190,153
Units in Unit Trusts – Unquoted		–	806,211	–	806,211
Unquoted shares		–	–	112,984	112,984
Government grant receivable	41	–	861,915	–	861,915
		48,353,048	1,791,103	112,984	50,257,135
Financial Liabilities					
Derivative liabilities held-for-risk management	28				
Forward foreign exchange contracts		–	105,741	–	105,741
		–	105,741	–	105,741

As Treasury Bills/Bonds are valued using Central Bank published rates, investments in Treasury Bills/Bonds are classified under Level 1.

59.4 Fair Value by Level of the Fair Value Hierarchy – Group

As at 31 December 2017	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Total LKR 000
Financial Assets					
Derivative assets held-for-risk management	27				
Forward foreign exchange contracts		–	66,440	–	66,440
Other financial assets held-for-trading	28				
Government of Sri Lanka Treasury Bonds		279,098	–	–	279,098
Equity securities – Quoted		31,828	–	–	31,828
Financial investments – Available for sale	31				
Government of Sri Lanka Treasury Bills and Bonds		37,746,039	–	–	37,746,039
Quoted ordinary shares		18,195,008	–	–	18,195,008
Units in Unit Trusts – Quoted		194,590	–	–	194,590
Units in Unit Trusts – Unquoted		–	644,862	–	644,862
Unquoted shares		–	–	85,555	85,555
Government grant receivable	41	–	642,583	–	642,583
		56,446,563	1,353,885	85,555	57,886,003
Financial Liabilities					
Derivative liabilities held-for-risk management	28				
Forward foreign exchange contracts		–	367,435	–	367,435
		–	367,435	–	367,435

As at 31 December 2016	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Total LKR 000
Financial Assets					
Derivative assets held-for-risk management	27				
Forward foreign exchange contracts		–	122,977	–	122,977
Financial investments – Available for sale	31				
Government of Sri Lanka Treasury Bills and Bonds		29,365,255	–	–	29,365,255
Quoted ordinary shares		18,797,640	–	–	18,797,640
Units in Unit Trusts – Quoted		190,153	–	–	190,153
Units in Unit Trusts – Unquoted		–	806,211	–	806,211
Unquoted shares		–	–	112,984	112,984
Government grant receivable	41	–	861,915	–	861,915
		48,353,048	1,791,103	112,984	50,257,135
Financial Liabilities					
Derivative liabilities held-for-risk management	28				
Forward foreign exchange contracts		–	105,741	–	105,741
		–	105,741	–	105,741

59.5 Fair Value of Financial Instruments Carried at Amortised Cost – Bank

The following table summarises the carrying amounts and the Bank's estimate of fair values of those financial assets and liabilities not presented on the Bank's statement of financial position at fair value. The fair values in the table below may be different from the actual amounts that will be received/paid on the settlement or maturity of the financial instrument. For certain instruments, the fair value may be determined using assumptions which are not observable in the market.

As at 31 December 2017	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Fair value LKR 000	Carrying amount LKR 000
Assets						
Cash and cash equivalents	25		4,106,225		4,106,225	4,106,225
Balances with Central Bank of Sri Lanka	26		10,557,688		10,557,688	10,557,688
Placements with banks	27		6,691,381		6,691,381	6,691,381
Loans to and receivables from banks	29		10,984,266		10,984,266	10,984,266
Loans to and receivables from other customers	30			208,781,978	208,781,978	213,675,866
Financial investments – Held-to-maturity	32	22,518,347	1,498,338		24,016,685	23,507,632
Due from subsidiaries				12,083	12,083	12,083
Other assets				2,775,741	2,775,741	2,775,741
Total		22,518,347	33,837,898	211,569,802	267,926,047	272,310,882
Liabilities						
Due to banks	44		9,640,735		9,640,735	9,640,735
Due to other customers	45			193,185,964	193,185,964	193,307,534
Other borrowing	46		41,319,591		41,319,591	41,319,591
Debt securities issued	47		24,435,795		24,435,795	24,443,767
Subordinated term debt	49		8,938,245		8,938,245	9,202,870
Other liabilities	48			4,078,984	4,078,984	4,078,984
Total		–	84,334,366	197,264,948	281,599,314	281,993,481

As at 31 December 2016	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Fair value LKR 000	Carrying amount LKR 000
Assets						
Cash and cash equivalents	25		4,330,934		4,330,934	4,330,934
Balances with Central Bank of Sri Lanka	26		8,062,567		8,062,567	8,062,567
Placements with banks	27		1,351,117		1,351,117	1,351,117
Loans to and receivables from banks	29		12,300,398		12,300,398	12,300,398
Loans to and receivables from other customers	30			183,514,729	183,514,729	185,784,979
Financial investments – Held to maturity	32	13,757,420	2,372,636		16,130,056	23,189,085
Other assets				2,562,978	2,562,978	2,562,978
Total		13,757,420	28,417,652	186,077,707	228,252,779	237,582,058
Liabilities						
Due to banks	44		18,103,587		18,103,587	18,103,587
Due to other customers	45			139,995,435	139,995,435	140,514,373
Other borrowing	46			40,751,346	40,751,346	40,751,346
Debt securities issued	47		28,077,060		28,077,060	29,179,185
Subordinated term debt	49		8,796,976		8,796,976	9,205,637
Other liabilities	48			3,850,826	3,850,826	3,850,826
Total		–	54,977,623	184,597,607	239,530,230	241,559,554

59.6 Fair Value of Financial Instruments Carried at Amortised Cost – Group

The following table summarises the carrying amounts and the Group's estimate of fair values of those financial assets and liabilities not presented on the Group's Statement of Financial Position at fair value. The fair values in the table below may be different from the actual amounts that will be received/paid on the settlement or maturity of the financial instrument. For certain instruments, the fair value may be determined using assumptions which are not observable in the market.

As at 31 December 2017	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Fair value LKR 000	Carrying amount LKR 000
Assets						
Cash and cash equivalents	**25**		**4,120,230**		**4,120,230**	**4,120,230**
Balances with Central Bank of Sri Lanka	**26**		**10,557,688**		**10,557,688**	**10,557,688**
Placements with banks	**27**		**6,712,131**		**6,712,131**	**6,712,131**
Loans to and receivables from banks	**29**		**10,984,266**		**10,984,266**	**10,984,266**
Loans to and receivables from other customers	**30**			**208,781,978**	**208,781,978**	**213,675,866**
Financial investments – Held to maturity	**32**	**22,518,347**	**1,498,338**		**24,016,685**	**23,507,632**
Other assets				**2,804,798**	**2,804,798**	**2,804,798**
Total		**22,518,347**	**33,872,653**	**211,586,776**	**267,977,776**	**272,362,611**
Liabilities						
Due to banks	**44**		**9,640,735**		**9,640,735**	**9,640,735**
Due to other customers	**45**			**192,798,577**	**192,798,577**	**192,920,147**
Other borrowing	**46**			**41,290,874**	**41,290,874**	**41,290,874**
Debt securities issued	**47**		**24,435,795**		**24,435,795**	**24,443,767**
Subordinated term debt	**49**		**8,938,245**		**8,938,245**	**9,202,870**
Other liabilities	**48**			**4,195,940**	**4,195,940**	**4,195,940**
		–	**43,014,775**	**238,285,391**	**281,300,166**	**281,694,333**

As at 31 December 2016	Notes	Level 1 LKR 000	Level 2 LKR 000	Level 3 LKR 000	Fair value LKR 000	Carrying amount LKR 000
Assets						
Cash and cash equivalents	25		4,344,260		4,344,260	4,344,260
Balances with Central Bank of Sri Lanka	26		8,062,567		8,062,567	8,062,567
Placements with banks	27		1,415,985		1,415,985	1,415,985
Loans to and receivables from banks	29		12,300,398		12,300,398	12,300,398
Loans to and receivables from other customers	30			183,514,729	183,514,729	185,784,979
Financial investments – Held to maturity	32	13,757,420	2,372,636		16,130,056	23,189,085
Other assets				2,609,655	2,609,655	2,609,655
Total		13,757,420	28,495,846	189,124,384	228,377,650	237,706,929
Liabilities						
Due to banks	44		18,103,587		18,103,587	18,103,587
Due to other customers	45			139,364,164	139,364,164	140,219,872
Other borrowing	46			40,736,300	40,736,300	40,736,300
Debt securities issued	47		28,077,060		28,077,060	29,179,185
Subordinated term debt	49		8,796,976		8,796,976	9,205,637
Other liabilities	48			3,961,249	3,961,249	3,961,249
			54,977,623	184,061,717	239,039,341	241,405,830

Given below is the basis adopted by the Bank/Group in order to establish the fair values of the financial instruments.

59.7 Cash and Cash Equivalents and Placements with Banks

Carrying amounts of cash and cash equivalents and placements with banks approximates their fair value as these balances have a remaining maturity of less than three months from the reporting date.

59.8 Loans to and Receivables from Banks and Other Customers

59.8.1 Lease Rentals Receivable – Bank

The estimated fair value of lease rentals receivable is the present value of future cash flows expected to be received from such finance lease facilities calculated based on current interest rates for similar type of facilities. The finance lease portfolio is at fixed interest rates and the fair value calculated on this basis as at 31 December 2017 was LKR 15,531 million as against a carrying value of LKR 16,493 million. (As at 31 December 2016 – fair value calculated on this basis was LKR 14,412 million as against a carrying value of LKR 15,909 million).

59.8.2 Other Loans

Composition:

	%
Floating rate loan portfolio	56
Fixed rate loans	
– With remaining maturity less than one year	7
– Others	37
Total	100

Since the floating rate loans can be repriced monthly, quarterly and semi-annually in tandem with market rates fair value of these loans is approximately same as the carrying value. Carrying amount of fixed rate loans with a remaining maturity of less than one year approximates the fair value.

Based on the results of the fair value computed on the lease rentals receivable, it is estimated that the fair value of the other loans at fixed interest rates with maturity of more than one year is not materially different to its carrying value as at the reporting date.

59.9 Financial Investments – Held to Maturity

Fair value of the fixed rate debentures are based on prices quoted in the Colombo Stock Exchange, where there is an active market for quoted debentures.

Where there is no active market, fair value of the fixed rate debentures has been determined by discounting the future cash flows by the interest rates derived with reference to Government Treasury Bond rates with adjustments to risk premiums at the time of investment.

59.10 Due to Banks

Carrying value of amounts due to banks approximates their fair value as these balances have a remaining maturity of less than one year from the reporting date.

59.11 Due to Other Customers

The carrying value of deposits with a remaining maturity of less than one year approximates the fair value.

Fair values of deposits with a remaining maturity of more than one year is estimated using discounted cash flows applying current interest rates offered for deposits of similar remaining maturities.

The fair value of a deposit repayable on demand is assumed to be the amount payable on demand at the reporting date and the savings account balances are repriced frequently to match with the current market rates, therefore the demand and saving deposits carrying amounts are reasonable approximation to the fair values as at the reporting date.

59.12 Other Borrowings

This consists of borrowings sourced from multilateral and bilateral institutions. Seventy per cent of these borrowing are repriced either monthly, quarterly or semi-annually and rates are revised in line with changes in market rates. Hence the carrying value of these borrowings approximates the fair value.

The others at fixed rates which relates to borrowings on credit lines are based on interest rates which are specific to each refinancing arrangement and as such there are no comparable market rates. Hence, the fair value approximates the carrying value.

59.13 Debt Securities Issued

Debts issued comprise the USD notes issue and LKR debentures. Fair value of the USD notes are determined by reference to the bid and ask price quoted in the Singapore Stock Exchange. The LKR debentures are fair valued by reference to current Government Treasury Bond rates with a risk premium.

60 Financial Risk Management

60.1 Introduction and Overview

Bank has exposure to the following key risks from financial instruments:

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

This note presents information about the Bank's exposure to each of the above risks, the objectives, policies and processes for measuring and managing such risks.

Risk Management Framework

The Board of Directors has the overall responsibility for the establishment and oversight of the Bank's risk management framework. It has set up a Board Integrated Risk Management Committee (BIRMC) with three Non-Executive Directors including the Chairman, one Executive Director and Chief Risk Officer (CRO) as members. CRO represents at the BIRMC the supervision and the management of the broad risk categories including credit, liquidity market risk, and strategic risk. As per the Board approved Charter, BIRMC assists the Board to manage these risks prudently. Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and to monitor adherence to limits. Risk management policies and systems are reviewed at least annually to reflect changes in market conditions, business strategy, products and services offered.

60.2 Credit Risk

60.2.1 Qualitative Disclosures

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from Bank's loans and advances to customers and other banks and investment in debt securities. Management of credit risk includes the following elements:

1. Formulating credit policies in consultation with business units covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures and compliance with regulatory and statutory requirements.
2. Establishing the authorisation structure for the approval and renewal of credit facilities.
3. Limiting concentration of exposures to counterparties and industries.
4. Developing and maintaining Bank's risk grading models in order to categorise exposures according to the degree of risk of financial loss and to focus management on the attendant risks.
5. Independent risk assessment, monitoring, recommending and reporting by the IRMD.
6. Reviewing compliance through regular audits by internal audit.

60.2.2 Quantitative Disclosures

	BANK		GROUP	
As at	**31.12.2017 LKR 000**	31.12.2016 LKR 000	**31.12.2017 LKR 000**	31.12.2016 LKR 000
60.2.2.1 Loans to and Receivables from Other Customers				
Individually Impaired				
Gross amount	**6,762,473**	6,010,399	**6,762,473**	6,010,399
Allowance for impairment	**(5,388,754)**	(4,778,752)	**(5,388,754)**	(4,778,752)
Carrying amount	**1,373,719**	1,231,647	**1,373,719**	1,231,647
Collectively Impaired				
Gross amount	**3,013,772**	2,628,487	**3,013,772**	2,628,487
Allowance for impairment	**(2,244,951)**	(1,890,798)	**(2,244,951)**	(1,890,798)
Carrying amount	**768,821**	737,689	**768,821**	737,689
Past Due But Not Impaired				
Gross amount	**77,509,049**	60,879,323	**77,509,049**	60,879,323
Allowance for impairment	**–**	–	**–**	–
Carrying amount	**77,509,049**	60,879,323	**77,509,049**	60,879,323

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Neither Past Due Nor Impaired				
Gross amount	**134,024,277**	122,936,320	**134,024,277**	122,936,320
Allowance for impairment	**–**	–	**–**	–
Carrying amount*	**134,024,277**	122,936,320	**134,024,277**	122,936,320
Carrying amount – amortised cost	**213,675,866**	185,784,979	**213,675,866**	185,784,979

60.2.2.2 Loans to and Receivables from Banks

As at	BANK 31.12.2017 LKR 000	BANK 31.12.2016 LKR 000	GROUP 31.12.2017 LKR 000	GROUP 31.12.2016 LKR 000
Neither Past Due Nor Impaired				
Gross amount	**10,984,266**	12,300,398	**10,984,266**	12,300,398
Allowance for impairment	**–**	–	**–**	–
Carrying amount	**10,984,266**	12,300,398	**10,984,266**	12,300,398

60.2.2.3 Analysis of Security Values of Loans to and Receivables from Other Customers

As at	BANK Gross loan balance 31.12.2017 LKR 000	BANK Security value 31.12.2017 LKR 000	BANK Gross loan balance 31.12.2016 LKR 000	BANK Security value 31.12.2016 LKR 000	GROUP Gross loan balance 31.12.2017 LKR 000	GROUP Security value 31.12.2017 LKR 000	GROUP Gross loan balance 31.12.2016 LKR 000	GROUP Security value 31.12.2016 LKR 000
Against Individually Impaired								
Mortgages over property, plant and machinery	**1,436,747**	**1,380,943**	1,612,896	1,449,450	**1,436,747**	**1,380,943**	1,612,896	1,449,450
Others	**1,099,530**	**630**	596,865	510,898	**1,099,530**	**630**	596,865	510,898
Unsecured	**4,217,884**	**–**	3,714,601	–	**4,217,884**	**–**	3,714,601	–
Against Collectively Impaired								
Mortgages over property, plant and machinery	**1,099,966**	**2,468,887**	1,060,924	2,319,203	**1,099,966**	**2,468,887**	1,060,924	2,319,203
Others	**246,882**	**32,013**	218,186	14,665	**246,882**	**32,013**	218,186	14,665
Unsecured	**1,550,494**	**–**	1,239,662	–	**1,550,494**	**–**	1,239,662	–
Against Past Due But Not Impaired								
Mortgages over property, plant and machinery	**36,423,748**	**85,688,766**	30,660,982	70,102,950	**36,423,748**	**85,688,766**	30,660,982	70,102,950
Others	**23,163,025**	**7,414,791**	17,520,717	5,618,646	**23,163,025**	**7,414,791**	17,520,717	5,618,646
Unsecured	**9,919,502**	**–**	6,965,357	–	**9,919,502**	**–**	6,965,357	–

As at	BANK				GROUP			
	Gross loan balance 31.12.2017 LKR 000	**Security value 31.12.2017 LKR 000**	Gross loan balance 31.12.2016 LKR 000	Security value 31.12.2016 LKR 000	**Gross loan balance 31.12.2017 LKR 000**	**Security value 31.12.2017 LKR 000**	Gross loan balance 31.12.2016 LKR 000	Security value 31.12.2016 LKR 000
Mortgages over property, plant and machinery	**43,732,774**	**117,966,759**	41,775,571	100,725,378	**43,732,774**	**117,966,759**	41,775,571	100,725,378
Treasury guarantee	**5,594,370**	**6,166,733**	5,874,580	7,180,759	**5,594,370**	**6,166,733**	5,874,580	7,180,759
Debt securities	**187,500**	**187,500**	517,500	517,500	**187,500**	**187,500**	517,500	517,500
Equity	**1,616,546**	**1,748,988**	1,767,950	1,937,591	**1,616,546**	**1,748,988**	1,767,950	1,937,591
Others	**42,412,026**	**11,484,079**	37,513,754	9,480,430	**42,412,026**	**11,484,079**	37,513,754	9,480,430
Unsecured	**32,115,203**	**–**	25,505,832	–	**32,115,203**	**–**	25,505,832	–
Total	**204,816,197**	**234,540,089**	176,545,377	199,857,470	**204,816,197**	**234,540,089**	176,545,377	199,857,470

The above analysis does not include balances relating to lease rentals receivable.

60.3 Liquidity Risk

60.3.1 Qualitative Disclosures

Liquidity risk is the risk that the Bank will not have sufficient financial resources to meet Bank's obligations as they fall due. This risk arises from mismatches in the timing of cash flows.

Management of liquidity risk includes the following elements:

a. Taking steps to ensure, as far as possible, that the Bank will always have sufficient financial resources to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

b. The Asset and Liability Committee (ALCO) is mandated to execute liquidity management policies, procedures and practices approved by the Board of Directors, effectively.

c. Monitoring of potential liquidity requirements and availability using the maturity analysis and cash flow forecast under normal and stressed conditions using a flow approach.

d. Monitoring the Group's liquidity through the Liquid Assets Ratio (statutory minimum is currently 20%) and Liquidity Coverage Ratios using a stock approach.

e. Effecting threshold limits relevant for liquidity management as part of the overall risk limits system of the Bank.

60.3.2 Quantitative Disclosures

Regulatory Liquidity (Bank)	31.12.2017	31.12.2016
Statutory liquid assets (LKR'000)	71,672,283	59,259,909
Statutory liquid assets ratio (mininum requirement 20%)		
Domestic banking unit (%)	24.34	24.56
Off-shore banking unit (%)	67.7	73.2
Liquidity Coverage Ratio (minimum requirement 80% in 2017 and 70% in 2016)		
All currencies (%)	108.5	168.8
Rupee only (%)	127.8	197.3

63.3.2.1 Maturity Profile of Financial Liabilities of the Bank

As at 31 December 2017	Carrying Amount	Total	Up to 3 months		3 to 12 months		1 to 3 years		3 to 5 years		>5 years	
	LKR 000	LKR 000	LKR 000	%	LKR 000	%	LKR 000	%	LKR 000	%	LKR 000	%
Liabilities with contractual maturity (Interest bearing liabilities)												
Due to banks	9,636,351	9,642,565	110,083	1	7,530,736	78	2,001,746	21	–	–	–	–
Due to other customers	188,838,665	189,024,016	78,004,690	41	59,135,540	31	10,401,732	6	9,459,778	5	32,022,276	17
Other Borrowings	41,319,591	41,322,672	1,591,024	4	3,402,175	8	11,548,027	28	11,678,491	28	13,102,955	32
Subordinated term debts	9,202,870	9,211,816	–	–	–	–	2,103,367	23	7,108,449	77	–	–
Debt securities issued	24,443,767	24,467,481	–	–	15,559,280	64	8,908,201	36	–	–	–	–
	273,441,244	273,668,550	79,705,797		85,627,731		34,963,073		28,246,718		45,125,231	
Other liabilities (Non-interest bearing liabilities)												
Due to banks	4,384	4,384	4,384	100	–	–	–	–	–	–	–	–
Derivative financial instruments	367,435	367,435	367,435	100	–	–	–	–	–	–	–	–
Due to other customers	4,468,869	4,468,869	1,874,658	42	1,539,215	34	–	–	–	–	1,054,996	24
Current tax payable	633,636	485,418	485,418	100	–	–	–	–	–	–	–	–
Deferred tax liability	1,194,027	1,003,444	1,003,444	100	–	–	–	–	–	–	–	–
Government Grant -deferred Income	654,583	654,583	–	–	654,583	100	–	–	–	–	–	–
Other liabilities	4,466,398	3,933,488	2,087,933	53	1,459,171	37	38,984	1	38,984	1	308,416	8
Total equity	47,876,766	34,526,467	–	–	–	–	–	–	–	–	34,526,467	
	59,666,098	45,444,088	5,823,272		3,652,969		38,984		38,984		35,889,879	
Total Equity and Liabilities	333,107,342	319,112,638	85,529,069		89,280,700		35,002,057		28,285,702		81,015,110	

63.3.2.2 Maturity Profile of Financial Liabilities of the Group

As at 31 December 2017	Carrying Amount	Total	Up to 3 months		3 to 12 months		1 to 3 years		3 to 5 years		>5 years	
	LKR 000	LKR 000	LKR 000	%	LKR 000	%	LKR 000	%	LKR 000	%	LKR 000	%
Liabilities with contractual maturity (Interest bearing liabilities)												
Due to banks	9,636,351	9,642,565	110,083	1	7,530,736	78	2,001,746	21	–	–	–	–
Due to other customers	188,451,278	188,636,629	77,617,303	41	59,135,540	31	10,401,732	6	9,459,778	5	32,022,276	17
Other Borrowings	41,290,874	41,293,955	1,562,307	4	3,402,175	8	11,548,027	28	11,678,491	28	13,102,955	32
Subordinated term debts	9,202,870	9,211,816	–	–	–	–	2,103,367	23	7,108,449	77	–	–
Debt securities issued	24,443,767	24,467,481	–	–	15,559,280	64	8,908,201	36	–	–	–	–
	273,025,140	273,252,446	79,289,693		85,627,731		34,963,073		28,246,718		45,125,231	
Other liabilities (Non-interest bearing liabilities)												
Due to banks	4,384	4,384	4,384	100	–	–	–	–	–	–	–	–
Derivative financial instruments	367,435	367,435	367,435	100	–	–	–	–	–	–	–	–
Due to other customers	4,468,869	4,468,869	1,874,658	42	1,539,215	34	–	–	–	–	1,054,996	24
Current tax payable	655,488	507,270	507,270	100	–	–	–	–	–	–	–	–
Deferred tax liability	1,232,478	1,041,895	1,041,895	100	–	–	–	–	–	–	–	–
Government Grant -deferred Income	654,583	654,583	–	–	654,583	100	–	–	–	–	–	–
Other liabilities	4,657,628	4,124,718	2,126,179	52	1,497,417	36	77,230	2	77,230	2	346,662	8
Total equity	49,401,857	36,051,558	–	–	–	–	–	–	–	–	36,051,558	
	61,442,722	47,220,712	5,921,821		3,691,215		77,230		77,230		37,453,216	
Total Equity and Liabilities	334,467,862	320,473,158	85,211,514		89,318,946		35,040,303		28,323,948		82,578,447	

60.4 Market Risk

60.4.1 Qualitative Disclosures

Market risk is the possibility of losses arising from changes in the value of a financial instrument as a result of changes in market variables, such as interest rates, equity prices, foreign exchange rates and commodity prices which will affect the Bank's income or the value of its holdings of financial instruments. The objective of the Bank' s market risk management is to manage and control market risk exposures within acceptable parameters, in order to ensure the Bank' s solvency and the income growth, while optimising the return on risk.

60.4.1.1 Management of Market Risks

The following policy frameworks stipulate the policies and practices for management, monitoring and reporting of market risk:

a. Market risk management framework

b. ALCO charter

c. Treasury trading guidelines and limits system

d. Treasury manual

e. Overall risk limits for market risk management

f. New product development policy

Overall authority for managing market risk is vested with the Board of Directors through the Board Integrated Risk Management Committee (BIRMC). The operational authority for managing market risk is vested with ALCO. Foreign exchange risk is managed within approved limits and segregation of reporting responsibilities of Treasury Front Office, Middle Office and Back Office.

Exposure to market risk arises from two sources viz trading portfolios from positions arising from market-making activities, and non-trading portfolios from positions arising from financial investments designated as available for sale (AFS) and held to maturity and from derivatives held-for-risk management purposes.

60.4.2 Quantitative Disclosures

In the case of interest rate and foreign exchange risk the following analysis is in respect of DFCC Bank PLC.

60.4.2.1 Interest Rate Risk – DFCC

60.4.2.1.1 Duration Analysis as at 31 December 2017

Portfolio	Face value LKR 000	Mark-to-market value LKR 000	Duration	Interpretation of duration
Government securities trading portfolio	250,000.00	271,381.20	5.49%	Portfolio value will decline approximately by 5.49% as a result of 1% increase in the interest rates.
Treasury Securities AFS portfolio	37,564,690	37,222,299	1.60%	Portfolio value will decline approximately by 1.60% as a result of 1% increase in the interest rates.

Market risk exposure for interest rate risk in the Trading portfolio as at 31 December 2017 is depicted by duration of 5.49%.

This level of interest rate risk exposure can be interpreted as a possible potential loss in the marked-to-market value amounting to LKR 14.9 million. in case, the market interest rates mark a parallel upward shift of 1%.

Therefore maximum holding period is restricted to 91 days for the Trading Portfolio.

Market risk exposure for interest rate risk in the AFS portfolio as at 31 December 2017 is depicted by duration of 1.60%. This level of interest rate risk exposure in the AFS portfolio can be interpreted as a possible potential loss in the marked-to-market value amounting to LKR 596.3 million, as at 31 December 2017

60.4.2.1.2 Potential Impact to NII Due to Change in Market Interest Rates

Overall up to the 12-month time bucket, DFCC carried a net liability sensitive position. This liability sensitivity will vary for each time bucket up to the 12-month period. The interest rate risk exposure as at 31 December 2017 is quantified based on the assumed change in the interest rates for each time period and is given in table below:

	0 to 1 month LKR 000	Over 1 – up to 3 months LKR 000	Over 3 – up to 6 months LKR 000	Over 6 – up to 12 months LKR 000
Total interest-bearing assets	128,103,811	9,954,432	19,845,446	30,972,667
Total interest-bearing liabilities	73,289,039	53,465,749	53,659,162	30,460,078
Net rate sensitive assets (liabilities)	54,814,772	(43,511,317)	(33,813,716)	512,589
Assumed change in interest rates (%)	0.50%	1.00%	1.50%	2.00%
Impact	274,074	(398,854)	(380,404)	5,126
Total net impact if interest rates increase	–	–	–	(500,058)
Total net impact if interest rates decline	–	–	–	500,058

We have assumed that the assets and liabilities are re-priced at the beginning of each time bucket and have also taken into account the remaining time from the repricing date up to one year.

60.4.2.2 Forex Risk in Net Open Position (NOP)/Unhedged Position of DFCC

The following table indicates the DFCC's exchange rate risk exposure based on its size of the NOP/unhedged positions in the foreign currency assets/liabilities. By 31 December 2017, DFCC carried a USD equivalent net open/unhedged "Oversold" position of LKR 65.6 million. The impact of exchange rate risk is given below:

	Amount
Net exposure – USD equivalent	(427,000)
Value of position in LKR 000	(65,587)
Exchange rate (USD/LKR) as at 31 December 2017	153.60
Possible potential loss to DFCC – LKR 000	
If Exchange rate (USD/LKR) depreciates by 1%	(656)
If exchange rate depreciates by 10%	(6,559)
If exchange rate depreciates by 15%	(9,838)

The estimated potential exchange loss is off set by the interest gain due to interest differential between LKR and the respective foreign currencies.

60.4.2.3 Equity Price Risk

Equity prices risk is part of market risk which is defined as the risk of possible losses arising from the equity market investments due to changes in the market prices of the invested shares. The Bank is exposed to equity prices risk through its investments in the equity market which has been shown in the trading and AFS portfolio.

Parameter	**Position as at 31 December 2017 LKR 000**	Position as at 31 December 2016 LKR 000
Marked-to-market value of the total quoted equity portfolio	**18,226,836**	18,797,640
Value-at-risk (under 99% probability for a quarterly time horizon)	**7.68%**	10.03%
Maximum possible loss of value in the marked-to-market value of the portfolio as indicated by the VAR over a quarterly period	**1,399,821**	1,885,403
Unrealised gains in the AFS equity portfolio reported in the fair value reserve	**12,668,565**	14,580,102

Equity price risk is quantified using the Value at Risk (VAR) approach based on the Historical Loss Method. Historical two-year portfolio returns is adopted to compute VAR as a measure of the equity prices risk exposure by DFCC Bank. This VAR computation for the equity AFS portfolio considers a quarterly time horizon.

60.4.2.4 Market Risk Exposures of DFCC Group for Regulatory Capital Assessment as at 31 December 2017

Under the Standardised Approach of Basel III with effect from July 2017, market risk exposures are quantified for regulatory capital purposes. The computation results as at 31 December 2017 are as follows:

	Risk-weighted assets LKR 000	Quantified possible exposure LKR 000
Interest rate risk	**7,872,233**	**885,626**
Equity prices risk	**111,709**	**12,567**
Foreign exchange and gold risk	**125,971**	**14,172**
Total	**8,109,913**	**912,365**

60.5 Operational Risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank relating to processes, personnel, technology and infrastructure and from external factors.

DFCC Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness whilst avoiding control procedures that restrict initiative and creativity.

60.5.1 Qualitative Disclosures

The following are included in the process of the operational risk management in DFCC Bank.

a. Monitoring of the Key Risk Indicators (KRIs) for the departments/functions under the defined threshold limits using a traffic light system. Develop Risk and Control Self-Assessments to identify the risk exposure of all processes.

b. Operational risk incident reporting system and the independent analysis of the incidents by the IRMD, and recognise necessary improvements in the systems, processes and procedures.

c. Analyse downtime of the critical systems, attrition information, exit interview comments and complaints to identify operational risks and recommend mitigating controls. The key findings of the analysis are evaluated at the ORMC and the BIRMC meetings in an operational risk perspective.

The primary responsibility for the development and implementation of controls to address operational risk lies with IRMD whilst implementation is assigned to Senior Management within each business unit. This responsibility is supported by the development of overall standards for management of operational risk in the following areas:

a. Requirements for appropriate segregation of duties, including independent authorisation of transactions

b. Requirements for reconciliation and monitoring of transactions

c. Compliance with regulatory and other legal requirements

d. Documentation of controls and procedures

e. Requirements for periodic assessment of operational risks faced and the adequacy of controls and procedures to address the identified risks

f. Requirements for reporting of operational losses and propose remedial action

g. Development of contingency plans

h. Training and professional development to establish ethics and business standards

j. Insurance covering risk due to threats arising from external and other events.

Compliance with the Bank's standards is supported by a programme of periodic reviews undertaken by internal audit. The results of internal audit reviews are discussed with the business unit to which they relate, with summaries submitted to the Audit Committee and Senior Management.

60.6 Capital Management

60.6.1 Qualitative Disclosures

DFCC Bank PLC manages its capital at Bank and Group level considering both regulatory requirement and risk exposures. Its regulatory capital position is analysed by the BIRMC on a quarterly basis and recommendations and decisions are made accordingly. The Group capital management goals are as follows:

a. Ensure regulatory minimum capital adequacy requirements are not compromised.

b. Bank to maintain its international and local credit rating and to ensure that no downgrading occurs as a result of deterioration of risk capital of the Bank.

c. Ensure above industry average Capital Adequacy Ratio is maintained.

d. Ensure maintaining of quality capital.

e. Ensure capital impact of business decisions are properly assessed and taken into consideration during product planning and approval process.

f. Ensure capital consumption by business actions are adequately priced.

Central Bank of Sri Lanka sets and monitors regulatory capital requirement on both consolidated and solo basis. The Bank is required to comply with the provisions of the Basel II and commencing from July 2017 the Basel III requirements in respect of regulatory capital. The Bank currently uses the standardised approach for credit risk and market risk and basic indicator approach for operational risk.

The Basel III capital regulations, which are planned to be implemented on a phased in basis by 2019 starting from mid 2017, will continue to be based on the three-mutually reinforcing Pillars introduced under Basel II, i.e., minimum capital requirement, supervisory review process and market discipline. Basel III focuses on increasing the quality and quantity of capital especially the Core Capital, through redefining the common equity capital and introducing new capital buffers such as the Capital Conservation Buffer and a Capital Surcharge on Domestic Systematically Important Banks. DFCC Bank started reporting capital computations under the Basel III requirements from mid 2017 as per the regulatory requirements.

Regulatory capital comprises Tier I capital and Tier II capital. The Bank's policy is to maintain a strong capital base so as to ensure investor, creditor and market confidence to sustain future development of the business.

DFCC Bank and its Group have complied with the minimum capital requirements imposed by the Central Bank of Sri Lanka throughout the year.

60.6.2 Key Regulatory Ratios – Capital

As at	31.12.2017		31.12.2016	
	Bank	**Group**	**Bank**	Group
Regulatory capital (LKR 000)				
Common equity Tier 1	**33,017,170**	**34,211,431**	**N/A**	N/A
Tier 1 capital	**33,017,170**	**34,211,431**	**N/A**	N/A
Total capital	**41,993,352**	**43,187,613**	**N/A**	N/A
Regulatory capital ratios (%)				
Common equity Tier 1 capital ratio (minimum requirement – 5.75%)	**12.68%**	**13.09%**	**N/A**	N/A
Tier 1 capital ratio (minimum requirement – 7.25%)	**12.68%**	**13.09%**	**N/A**	N/A
Total capital ratio (minimum requirement – 11.25%)	**16.13%**	**16.53%**	**N/A**	N/A

Basel III Computation of Capital Ratios

As at	31.12.2017	
	Bank LKR 000	Group LKR 000
Common equity Tier 1 (CET 1) capital after adjustments	**33,017,170**	**34,211,431**
Common equity Tier 1 (CET 1) capital	**38,035,888**	**41,884,674**
Equity capital (stated capital)/assigned capital	**4,715,814**	**4,715,814**
Reserve fund	**2,224,275**	**2,224,275**
Published retained earnings/ (accumulated retained losses)	**9,607,311**	**17,357,048**
Published accumulated Other Comprehensive Income (OCI)	**3,457,808**	**3,807,698**
General and other disclosed reserves	**13,779,839**	**13,779,839**
Unpublished current year's profit/loss and gains reflected in OCI	–	–
Ordinary shares issued by consolidated banking and financial subsidiaries of the Bank and held by third parties	–	–
Total adjustments to CET 1 capital	**5,018,718**	**7,673,243**
Goodwill (net)	–	**156,226**
Intangible assets (net)	**498,084**	**502,411**
Others (investment in capital of banks and financial institutions)	**4,520,634**	**7,014,606**
Additional Tier 1 (AT1) capital after adjustments	–	–
Additional Tier 1 (AT1) capital	–	–
Qualifying Additional Tier 1 capital instruments	–	–
Instruments issued by consolidated banking and financial subsidiaries of the Bank and held by third parties	–	–
Total Adjustments to AT1 capital	–	–
Investment in own shares	–	–
Others (specify)	–	–
Tier 2 capital after adjustments	**8,976,182**	**8,976,182**
Tier 2 capital	**8,976,182**	**8,976,182**
Qualifying Tier 2 capital instruments	**8,008,628**	**8,008,628**
Revaluation gains	–	
Loan Loss Provisions	**967,554**	**967,554**
Instruments issued by consolidated banking and financial subsidiaries of the Bank and held by third parties	–	–
Total Adjustments to Tier 2	–	–
Investment in own shares	–	–
Others (specify)	–	–
CET1 capital	**33,017,170**	**34,211,431**
Total Tier 1 capital	**33,017,170**	**34,211,431**
Total capital	**41,993,352**	**43,187,613**

Other Disclosure Requirements Under the Prescribed Format Issued by the Central Bank of Sri Lanka for Preparation of Annual Financial Statements of Licensed Commercial Banks

Disclosure Requirements		Description	Page No.
1.	**Information about the Significance of Financial Instruments for Financial Position and Performance**		
1.1	Statement of Financial Position		
1.1.1	Disclosures on categories of financial assets and financial liabilities.	Note 23 to the financial statements Analysis of Financial Instruments by Measurement basis	183
1.1.2	Other Disclosures	Not designated.	
	i. Special disclosures about financial assets and financial liabilities designated to be measured at fair value through profit or loss, including disclosures about credit risk and market risk, changes in fair values attributable to these risks and the methods of measurement.	Note 5.3.1 – Designated fair value Please refer Integrated risk management report	166
	ii. Reclassifications of financial instruments from one category to another.	Significant accounting policies: Note 5.3.3 – Reclassification of financial instruments	166
	iii. Information about financial assets pledged as collateral and about financial or non-financial assets held as collateral.	Note 46.1 – Assets pledged as security	210
	iv. Reconciliation of the allowance account for credit losses by class of financial assets.	Notes to the financial statements: Note 30.2 – Movement in specific and collective allowance for impairment	192
	v. Information about compound financial instruments with multiple embedded derivatives.	The Bank does not have compound financial instruments with multiple embedded derivatives.	
	vi. Breaches of terms of loan agreements.	None	
1.2	Statement of Comprehensive Income		
1.2.1	Disclosures on items of income, expense, gains and losses.	Notes 9 – 21 to the financial statements:	172-182
1.2.2	Other Disclosures		
	i. Total interest income and total interest expense for those financial instruments that are not measured at fair value through profit and loss.	Notes to the financial statements: Note 10 – Interest income	173
	ii. Fee income and expense.	Note 12 to the financial statements: Net fee and commission income	174
	iii. Amount of impairment losses by class of financial assets.	Note 16 to the financial statements: Impairment for loans and other losses.	177
	iv. Interest income on impaired financial assets.		
1.3	Other Disclosures		
1.3.1	Accounting policies for financial instruments.	Significant accounting policies: Note 5.3 – Financial instruments – initial recognition, classification and subsequent measurement.	166
1.3.2	Information on hedge accounting.	The Bank does not adopt hedge accounting.	
1.3.3	Information about the fair values of each class of financial asset and financial liability, along with:		
	i. Comparable carrying amounts.	Notes to the financial statements: Note 59.1 to 59.4 – Fair value measurement	228-233
	ii. Description of how fair value was determined.	Notes to the financial statements: Note 59.1	
	iii. The level of inputs used in determining fair value.	Notes to the financial statements: Note 59.7 to 59.13	233-234
	iv. a. Reconciliations of movements between levels of fair value measurement hierarchy. b. Additional disclosures for financial instruments that fair value is determined using level 3 inputs.	There were no movements between levels of fair value hierarchy during the period under review.	
	v. Information if fair value cannot be reliably measured.	Notes to the financial statements: Note 59.7 to 59.13	233-234

Disclosure Requirements	Description	Page No.
2. Information about the Nature and Extent of Risks Arising from Financial Instruments		
2.1 Qualitative Disclosures		
2.1.1 Risk exposures for each type of financial instrument.	Please refer the report on Integrated risk management.	
2.1.2 Management's objectives, policies, and processes for managing those risks.	Please refer the section relating to Integrated risk managements objectives, policies and processes.	
2.1.3 Changes from the prior period.	Notes to the financial statements: Note 57.1 – Reclassification of comparative figures	227
2.2 Quantitative Disclosures		
2.2.1 Summary of quantitative data about exposure to each risk at the reporting date.	Please refer the section relating to Integrated risk managements objectives, policies and processes. Notes to the Financial Section Note 60	
2.2.2 Disclosures about credit risk, liquidity risk, market risk, operational risk, interest rate risk and how these risks are managed.	Please refer the section relating to Integrated risk managements objectives, policies and processes. Notes to the Financial Statements Note 60	234
i. Credit Risk		
a. Maximum amount of exposure (before deducting the value of collateral), description of collateral, information about credit quality of financial assets that are neither past due nor impaired and information about credit quality of financial assets.	Note 30.1.3 on industry analysis.	191
b. For financial assets that are past due or impaired, disclosures on age, factors considered in determining as impaired and the description of collateral on each class of financial asset.	Note 30.1.3 on industry analysis. Note 60.2.2.1 & 60.2.2.3 on loans and advances and impairment analysis.	191 235-236
c. Information about collateral or other credit enhancements obtained or called.	Note 60.2.2.3 Analysis of Security Values of Loans to and Receivables from other customers	236
d. For other disclosures, please refer Banking Act Direction No. 7 of 2011 on Integrated Risk Management Framework for Licensed Banks (Section H).	The section on 'Integrated risk management'. Note 60.2 Credit Risk	235
ii. Liquidity Risk		
a. A maturity analysis of financial liabilities.	Notes to the financial statements: Note 60.3.2.1 and 60.3.2.2 Maturity analysis of financial liabilities.	238-239
b. Description of approach to risk management.	The section on "Integrated risk management".	
c. For other disclosures, please refer Banking Act Direction No. 7 of 2011 on Integrated Risk Management Framework for Licensed Banks (Section H).	Please refer the section on "Integrated risk management". Note 60.3 Liquidity Risk	237
iii. Market Risk		
a. A sensitivity analysis of each type of market risk to which the entity is exposed.	Notes to the financial statements: Note 60.4 – Market risk	239
b. Additional information, if the sensitivity analysis is not representative of the entity's risk exposure.	None	
c. For other disclosures, please refer Banking Act Direction No. 7 of 2011 on Integrated Risk Management Framework for Licensed Banks (Section H).	Please refer the section on "Integrated risk management". Note 60.4 Market Risk	239
iv. Operational Risk		
Please refer Banking Act Direction No. 7 of 2011 on Integrated Risk Management Framework for Licensed Banks (Section H).	Notes to the financial statements: Note 60.5 – Operational risk	242

Disclosure Requirements	Description	Page No.
v. Equity Risk in the Banking Book		
a. Qualitative Disclosures		
• Differentiation between holdings on which capital gains are expected and those taken under other objectives including for relationship and strategic reasons.	Notes to the financial statements: Note 60.4.2.3 – Equity price risk	241
• Discussion of important policies covering the valuation and accounting of equity holdings in the banking book.	Note 4.1, 4.2 & 4.3	164-165
b. Quantitative Disclosures		
• Value disclosed in the statement of financial position of investments, as well as the fair value of those investments; for quoted securities, a comparison to publicly quoted share values where the share price is materially different from fair value. • The types and nature of investments. The cumulative realised gains/(losses) arising from sales and liquidations in the reporting period.	Notes to the financial statements: Note 31 – Financial investments – Available-for-sale Note 33 – Investments in subsidiaries Note 34 – Investments in associates Note 14 – Net gain/loss from financial investments	 192 198 199 175
vi. Interest Rate Risk in the Banking Book		
a. Qualitative Disclosures		
• Nature of interest rate risk in the banking book (IRRBB) and key assumptions.	Please refer the section on 'Integrated risk management'.	
b. Quantitative Disclosures		
• The increase/(decline) in earnings or economic value (or relevant measure used by management) for upward and downward rate shocks according to management's method for measuring IRRBB, broken down by currency (as relevant).	Please refer the section on 'Integrated risk management' and Note 60.4.2.1.2	240
2.2.3 Information on concentrations of risk.	Please refer the section on 'Integrated risk management'.	
3. Other Disclosures		
3.1 Capital		
3.1.1 Capital Structure		
i. Qualitative Disclosures.		
Summary information on the terms and conditions of the main features of all capital instruments, especially in the case of innovative, complex or hybrid capital instruments.	Notes to the financial statements: Note 60.6.2	243
ii. Quantitative Disclosure		
a.The amount of Tier 1 capital, with separate disclosure of: • Paid-up share capital/common stock • Reserves • Non-controlling interests in the equity of subsidiaries • Innovative instruments • Other capital instruments • Deductions from Tier 1 capital b. The total amount of Tier 2 and Tier 3 capital c. Other deductions from capital d. Total eligible capital	Notes to the financial statements: Note 60.6.2 - Financial risk management	243
3.1.2 Capital adequacy		
i. Qualitative Disclosures		
A summary discussion of the Bank's approach to assessing the adequacy of its capital to support current and future activities.	Please refer the section on 'Integrated risk management'.	
ii. Quantitative Disclosures		
a. Capital requirements for credit risk, market risk and operational risk	Please refer the section on 'Integrated risk management'.	
b. Total and Tier 1 capital ratio	Please refer the section on 'Integrated risk management'.	

Quantitative Disclosures as per Schedule III of Banking Act Direction No. 01 of 2016, Capital Requirements under Basel III

Basel III Computation of Liquidity Coverage Ratio – All Currencies

As at	Amount (LKR 000)			
	31.12.2017		31.12.2016	
	Total un-weighted value	**Total weighted value**	Total un-weighted value	Total weighted value
Total Stock of High-Quality Liquid Assets (HQLA)	**57,330,169**	**56,380,414**	33,793,942	32,777,711
Total Adjusted Level 1A Assets	**55,311,905**	**55,311,905**	31,627,816	31,627,816
Level 1 Assets	**55,311,905**	**55,311,905**	31,627,816	31,627,816
Total Adjusted Level 2A Assets	**169,650**	**144,203**	190,950	162,308
Level 2A Assets	**169,650**	**144,203**	190,950	162,308
Total Adjusted Level 2 B Assets	**1,848,614**	**924,307**	1,975,175	987,588
Level 2B Assets	**1,848,614**	**924,307**	1,975,175	987,588
Total Cash Outflows	**297,199,823**	**72,429,675**	234,880,834	27,389,642
Deposits	**110,539,102**	**11,053,910**	139,634,635	13,963,463
Unsecured wholesale funding	**85,471,888**	**50,626,218**	5,524,273	5,524,273
Secured funding transactions	**3,193,156**	–	15,314,274	–
Undrawn portion of committed (irrevocable) facilities and other contingent funding obligations	**95,512,713**	**8,266,582**	72,266,783	5,761,037
Additional Requirements	**2,482,964**	**2,482,964**	2,140,870	2,140,870
Total cash inflows	**35,261,499**	**20,470,813**	16,480,735	7,967,339
Maturing secured lending transactions backed by collateral	**178,770**	**89,385**	70,203	35,102
Committed facilities	**1,000,000**	–	1,000,000	–
Other inflows by counterparty which are maturing within 30 days	**33,543,891**	**20,314,000**	14,251,905	7,808,813
Operational deposits	**470,422**	–	1,034,756	–
Other cash inflows	**68,417**	**67,428**	123,871	123,424
Liquidity Coverage Ratio (%) (Stock of High Quality Liquid Assets/Total Net Cash Outflows over the Next 30 Calendar Days)* 100		**108.51**		168.76

Basel III Computation of Liquidity Coverage Ratio – LKR Only

As at	Amount (LKR 000)			
	31.12.2017		**31.12.2016**	
	Total un-weighted value	**Total weighted value**	Total un-weighted value	Total weighted value
Total Stock of High-Quality Liquid Assets (HQLA)	**57,252,785**	**56,303,031**	33,769,998	32,753,768
Total Adjusted Level 1A Assets	**55,234,521**	**55,234,521**	31,603,873	31,603,873
Level 1 Assets	**55,234,521**	**55,234,521**	31,603,873	31,603,873
Total Adjusted Level 2A Assets	**169,650**	**144,203**	190,950	162,308
Level 2A Assets	**169,650**	**144,203**	190,950	162,308
Total Adjusted Level 2B Assets	**1,848,614**	**924,307**	1,975,175	987,588
Level 2B Assets	**1,848,614**	**924,307**	1,975,175	987,588
Total Cash Outflows	**223,260,953**	**57,527,010**	181,344,999	21,827,013
Deposits	**90,452,711**	**9,045,271**	111,289,090	11,128,909
Unsecured wholesale funding	**63,718,277**	**41,175,092**	4,740,000	4,740,000
Secured funding transactions	**3,193,156**	–	15,314,274	–
Undrawn portion of committed (irrevocable) facilities and other contingent funding obligations	**63,775,251**	**5,185,089**	47,964,329	3,920,798
Additional requirements	**2,121,558**	**2,121,558**	2,037,306	2,037,306
Total cash inflows	**25,759,051**	**13,486,662**	11,439,661	5,222,282
Maturing secured lending transactions backed by collateral	**178,770**	**89,385**	70,203	35,102
Committed facilities	**1,000,000**	–	1,000,000	–
Other inflows by counterparty which are maturing within 30 days	**24,578,304**	**13,396,288**	10,368,565	5,186,734
Operational deposits	–	–	–	–
Other cash inflows	**1,977**	**988**	894	447
Liquidity Coverage Ratio (%) (Stock of High Quality Liquid Assets/Total Net Cash Outflows over the Next 30 Calendar Days)* 100		**127.84**		197.26

As at	**31.12.2017**		31.12.2016	
	Bank	**Group**	Bank	Group
Regulatory liquidity				
Statutory liquid assets (lkr 000)	**71,672,283**	**N/A**	59,259,909	N/A
Statutory liquid assets ratio (20%)				
Domestic banking unit (%)	**24.34%**	**N/A**	24.56%	N/A
Off-shore banking unit (%)	**67.70%**	**N/A**	73.20%	N/A

Maturity of Financial Assets and Financial Liabilities

Bank as at 31 December 2017

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Total* LKR 000
Financial Assets								
Cash and cash equivalents	4,106,225							4,106,225
Balances with Central Bank of Sri Lanka	10,557,688							10,557,688
Placement with banks	6,691,381							6,691,381
Reverse repurchase agreements	–							–
Derivative financial instruments	66,440							66,440
Financial assets – held for trading	–	7,172	549				271,374	279,095
Loans to receivables from banks	786,286	1,364,645	952,263	9,808	6,339,072	1,536,000		10,988,074
Loans to receivables from other customers	20,727,415	19,308,936	13,822,894	12,881,088	34,375,820	50,212,104	59,345,388	210,673,645
Financial assets – available for sale	1,938,150	836,695	10,133,632	10,756,311	3,261,869	4,202,149	12,940,625	44,069,431
Financial assets – held to maturity	204,111	973,548	817,554	2,542,722	6,104,030	11,420,684	1,451,159	23,513,808
Other assets	2,042,795	254,972	164,728	790,507	279,972	433,590	1,736,059	5,702,623
Total financial assets	47,120,491	22,745,968	25,891,620	26,980,436	50,360,763	67,804,527	75,744,605	316,648,410
Financial Liabilities								
Due to banks	68,965	45,501	2,871,692	4,659,044	2,001,746			9,646,948
Derivative financial instruments	367,435							367,435
Securities sold under repurchase agreements	3,193,156	1,322,489	27,022	3,397				4,546,064
Due to other customers	30,289,983	47,714,707	43,909,341	15,226,199	10,401,732	9,459,778	29,690,589	186,692,329
Debt issued and other borrowed funds	1,103,460	487,564	1,472,028	17,489,427	20,456,228	11,678,491	16,251,765	68,938,963
Dividend payable							47,318	47,318
Other liabilities	3,892,393	3,163,947	3,115,282	3,313,094	233,646	139,804	776,021	14,634,187
Total financial liabilities	38,915,392	52,734,208	51,395,365	40,691,161	33,093,352	21,278,073	46,765,693	284,873,244
Total net financial assets/(liabilities)	8,205,099	(29,988,240)	(25,503,745)	(13,710,725)	17,267,411	46,526,454	28,978,912	31,775,166
Contingencies								
Guarantees	16,571,273							16,571,273
Acceptance	1,545,458	2,559,024	1,829,954	8,233	11,520			5,954,189
Forward contracts		9,984,303	5,044,794	22,760,617	328,300			38,118,014
Documentary credit	2,333,711	5,788,172	662,801	359,235				9,143,919
Bills for collection	2,305,466							2,305,466
Total Contingencies	22,755,908	18,331,499	7,537,549	23,128,085	339,820	–	–	72,092,861

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Total* LKR 000
Commitments								
Undrawn overdrafts	**12,350,333**							**12,350,333**
Undrawn loans	**38,883,858**							**38,883,858**
Undrawn credit card limits	**585,502**							**585,502**
Undrawn indirect credit facilities	**10,510,442**							**10,510,442**
Capital commitments	**751,422**							**751,422**
Undrawn leases	**522,440**							**522,440**
Total Commitments	**63,603,997**	–	–	–	–	–		**63,603,997**
Total Commitments and Contingencies	**86,359,905**	**18,331,499**	**7,537,549**	**23,128,085**	**339,820**	–		**135,696,858**

** Represents the aggregate of the contractual maturities based on undiscounted cash flows.*

Bank as at 31 December 2016

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Total* LKR 000
Financial Assets								
Cash and cash equivalents	4,335,934							4,335,934
Balances with Central Bank of Sri Lanka	8,062,567							8,062,567
Placement with banks	1,351,117							1,351,117
Reverse repurchase agreements	1,000,000							1,000,000
Derivative financial instruments	122,977							122,977
Financial assets – held for trading	–							–
Loans to receivables from banks	705,780	4,708,313	3,984,302	33,621	2,882,671			12,314,687
Loans to receivables from other customers	14,587,474	12,985,037	6,909,033	10,439,270	26,675,967	40,788,377	57,202,195	169,587,353
Financial assets – available for sale	9,615,871	546,067	10,890,126	3,324,310	1,478,485	1,377,885	6,158,418	33,391,162
Financial assets – held to maturity	3,007,813	5,430,960	9,914,312	2,817,591	8,793,961	3,743,940	3,210,292	36,918,869
Other assets	2,727,570	633,976	301,237	1,030,046	214,747	340,437	780,580	6,028,593
Total financial assets	45,517,103	24,304,353	31,999,010	17,644,838	40,045,831	46,250,639	67,351,485	273,113,259

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Total* LKR 000
Financial Liabilities								
Due to banks	5,600,272	750,500		500,333	6,500,667			13,351,772
Derivative financial instruments	105,741							105,741
Securities sold under repurchase agreements	15,314,274	922,518	69,942	5,225				16,311,959
Due to other customers	24,607,724	31,100,991	33,172,443	12,753,679	7,327,950	6,011,841	21,238,712	136,213,340
Debt issued and other borrowed funds	998,300	5,852,654	1,473,877	6,904,141	22,472,482	11,058,121	17,219,846	65,979,421
Dividend payable							57,538	57,538
Other liabilities	3,349,477	2,265,617	2,397,989	2,958,117	192,806	118,168	792,152	12,074,326
Total financial liabilities	49,975,788	40,892,280	37,114,251	23,121,495	36,493,905	17,188,130	39,308,250	244,094,097
Total net financial assets/(liabilities)	(4,458,685)	(16,587,927)	(5,115,241)	(5,476,657)	3,551,926	29,062,509	28,043,235	29,019,162
Contingencies								
Guarantees	9,444,116							9,444,116
Acceptance	1,176,614	1,610,244	1,399,312	46,381	17,337			4,249,888
Forward contracts		1,320,734	17,877,698	7,505,700				26,704,132
Documentary credit	779,344	4,065,867	486,638	181,738				5,513,587
Bills for collection	3,148,059							3,148,059
Total Contingencies	14,548,133	6,996,845	19,763,648	7,733,819	17,337	–	–	49,059,782
Commitments								
Undrawn overdrafts	11,978,026							11,978,026
Undrawn loans	26,594,981							26,594,981
Undrawn credit card limits	565,740							565,740
Undrawn indirect credit facilities	12,400,027							12,400,027
Capital commitments	329,437							329,437
Undrawn leases	520,419							520,419
Total Commitments	52,388,630	–	–	–	–	–		52,388,630
Total Commitments and Comtingencies	66,936,763	6,996,845	19,763,648	7,733,819	17,337	–		101,448,412

** Represents the aggregate of the contractual maturities based on undiscounted cash flows.*

Maturity Gap Analysis of Foreign Currency Denominated Financial Assets and Financial Liabilities – USD

As at 31 December 2017	**Up to 1 Month USD 000**	**1-3 Months USD 000**	**3-6 Months USD 000**	**6-12 Months USD 000**	**1-3 Years USD 000**	**3-5 Years USD 000**	**Over 5 Years USD 000**	**Total USD 000**
Total assets	**64,483**	**29,634**	**15,313**	**1,980**	**48,855**	**39,970**	**259,724**	**459,959**
Total liabilities	**74,061**	**50,965**	**35,354**	**133,232**	**66,329**	**59,174**	**34,340**	**453,455**
Total net financial assets/(liabilities)	**(9,578)**	**(21,331)**	**(20,041)**	**(131,252)**	**(17,474)**	**(19,204)**	**225,384**	**6,504**

As at 31 December 2016	Up to 1 Month USD 000	1-3 Months USD 000	3-6 Months USD 000	6-12 Months USD 000	1-3 Years USD 000	3-5 Years USD 000	Over 5 Years USD 000	Total USD 000
Total assets	42,554	52,162	40,073	1,033	29,611	24,158	167,622	357,213
Total liabilities	82,832	29,500	45,093	23,624	135,679	20,858	14,522	352,108
Total net financial Assets/(liabilities)	(40,278)	22,662	(5,020)	(22,591)	(106,068)	3,300	153,100	5,105

Sensitivity of Financial Assets and Financial Liabilities

Bank as at 31 December 2017

	Up to 1 Month LKR 000	**1-3 Months LKR 000**	**3-6 Months LKR 000**	**6-12 Months LKR 000**	**1-3 Years LKR 000**	**3-5 Years LKR 000**	**Over 5 Years LKR 000**	**Non-interest Bearing LKR 000**	**Total LKR 000**
Financial Assets									
Cash and cash equivalents	**655,327**							**3,450,898**	**4,106,225**
Balances with Central Bank of Sri Lanka								**10,557,688**	**10,557,688**
Placements with banks	**6,691,381**								**6,691,381**
Derivative financial instruments								**66,440**	**66,440**
Financial assets – held for trading	**–**	**7,172**	**549**				**707,039**		**714,760**
Loans to & receivables from banks	**786,285**	**1,364,645**	**952,263**	**9,808**	**6,339,072**	**1,536,000**			**10,988,073**
Loans to and receivables from other customers	**118,551,359**	**7,678,804**	**8,163,974**	**17,702,281**	**22,549,741**	**14,456,335**	**19,917,642**	**4,007,064**	**213,027,200**
Financial assets – available for sale	**1,324,866**	**152,193**	**9,939,379**	**10,756,311**	**3,261,869**	**4,202,149**	**7,514,493**	**6,330,180**	**43,481,440**
Financial assets – held to maturity	**94,591**	**751,618**	**789,281**	**2,504,267**	**5,305,704**	**11,305,164**	**1,451,159**	**1,312,022**	**23,513,806**
Other assets								**6,098,846**	**6,098,846**
Total financial assets	**128,103,809**	**9,954,432**	**19,845,446**	**30,972,667**	**37,456,386**	**31,499,648**	**29,590,333**	**31,823,136**	**319,245,859**

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Non-interest Bearing LKR 000	Total LKR 000
Financial Liabilities									
Due to banks		1,500,000	2,850,000	4,000,000				74,967	8,424,967
Derivative financial instruments								367,435	367,435
Securities sold under repurchase agreements	4,399,347	1,370,312	34,132	3,434					5,807,225
Due to other customers	64,009,635	44,884,132	41,302,210	10,666,994	1,238,153	296,199	19,409,793	4,885,212	186,692,327
Debt issued and other borrowed funds	4,880,057	5,711,305	9,472,820	15,789,650	13,037,474	5,249,052	14,719,928		68,860,286
Dividend payable								47,338	47,338
Other liabilities								49,046,280	49,046,280
Total financial liabilities	73,289,039	53,465,749	53,659,162	30,460,078	14,275,627	5,545,251	34,129,721	54,421,231	319,245,858
Interest rate sensitivity gap	54,814,772	(43,511,317)	(33,813,716)	512,589	23,180,759	25,954,397	(4,539,388)	(22,598,095)	–

Bank as at 31 December 2016

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Non-interest Bearing LKR 000	**Total** LKR 000
Financial Assets									
Cash and cash equivalents	889,413							3,434,847	4,344,260
Balances with Central Bank of Sri Lanka								8,062,567	8,062,567
Placements with banks	1,351,117							64,868	1,415,985
Derivative financial instruments								122,977	122,977
Financial assets – held for trading									–
Loans to and receivables from banks	675,450	4,617,076	3,940,090	53,350	2,604,973				11,890,939
Loans to and receivables from other customers	116,050,716	6,283,736	5,116,762	8,833,491	21,648,751	9,080,556	13,422,936	3,269,092	183,706,040
Financial assets – available for sale	10,651,169	510,240	10,887,124	3,270,995	1,515,170	1,464,296	1,979,807		30,278,801
Financial assets – held to maturity	2,332,364	751,384	5,930,925	2,216,966	5,209,929	3,091,440	1,469,005	8,138,283	29,140,296
Other assets								5,251,057	5,251,057
Total financial assets	131,950,229	12,162,436	25,874,901	14,374,802	30,978,823	13,636,292	16,871,748	28,363,691	274,212,922

	Up to 1 Month LKR 000	1-3 Months LKR 000	3-6 Months LKR 000	6-12 Months LKR 000	1-3 Years LKR 000	3-5 Years LKR 000	Over 5 Years LKR 000	Non-interest Bearing LKR 000	**Total** LKR 000
Financial Liabilities									
Due to banks	10,093,225	750,500			7,215,936			43,926	18,103,587
Derivative financial instruments								103,564	103,564
Securities sold under repurchase agreements	12,464,980	922,518	69,942	5,225					13,462,665
Due to other customers	46,146,229	28,912,802	31,216,723	20,710,644	3,058,727	1,197,377	47,258	4,923,581	136,213,340
Debt issued and other borrowed funds	1,260,748	6,265,601	6,066,018	5,233,941	23,301,026	8,441,121	13,507,079	1,400	64,076,934
Dividend payable								60,828	60,828
Other liabilities								42,192,004	42,192,004
Total financial liabilities	69,965,182	36,851,421	37,352,683	25,949,810	33,575,689	9,638,498	13,554,337	47,325,303	274,212,922
Interest Rate Sensitivity Gap	61,985,047	(24,688,985)	(11,477,782)	(11,575,008)	(2,596,866)	3,997,794	3,317,411	(18,961,612)	–

Key Regulatory Ratios – Capital

As at	**31.12.2017**	
	Bank	**Group**
Regulatory capital (LKR 000)		
Common equity Tier 1	**33,017,170**	**34,211,431**
Tier 1 capital	**33,017,170**	**34,211,431**
Total capital	**41,993,352**	**43,187,613**
Regulatory capital ratios (%)		
Common equity Tier 1 capital ratio (minimum requirement – 5.75%)	**12.68%**	**13.09%**
Tier 1 capital ratio (minimum requirement – 7.25%)	**12.68%**	**13.09%**
Total capital ratio (minimum requirement – 11.25%)	**16.13%**	**16.53%**

Basel III Computation of Capital Ratios

As at	31.12.2017	
	Bank LKR 000	**Group LKR 000**
Common equity Tier 1 (CET 1) capital after adjustments	**33,017,170**	**34,211,431**
Common equity Tier 1 (CET 1) capital	**38,035,888**	**41,884,674**
Equity capital (stated capital)/assigned capital	**4,715,814**	**4,715,814**
Reserve fund	**2,224,275**	**2,224,275**
Published retained earnings/ (accumulated retained losses)	**13,858,152**	**17,357,048**
Published accumulated Other Comprehensive Income (OCI)	**3,457,808**	**3,807,698**
General and other disclosed reserves	**13,779,839**	**13,779,839**
Unpublished current year's profit/loss and gains reflected in OCI	–	–
Ordinary shares issued by consolidated banking and financial subsidiaries of the Bank and held by third parties	–	–

As at	31.12.2017	
	Bank LKR 000	Group LKR 000
Total adjustments to CET 1 capital	**5,018,718**	**7,673,243**
Goodwill (net)	–	**156,226**
Intangible assets (net)	**498,084**	**502,411**
Others (investment in capital of banks and financial institutions)	**4,520,634**	**7,014,606**
Additional Tier 1 (AT1) capital after adjustments	–	
Additional Tier 1 (AT1) capital	–	
Qualifying Additional Tier 1 capital instruments	–	
Instruments issued by consolidated banking and financial subsidiaries of the Bank and held by third parties	–	
Total Adjustments to AT1 capital	–	
Investment in own shares	–	
Others (specify)	–	
Tier 2 capital after adjustments	**8,976,182**	**8,976,182**
Tier 2 capital	**8,976,182**	**8,976,182**
Qualifying Tier 2 capital instruments	**8,008,628**	**8,008,628**
Revaluation gains	–	
Loan Loss Provisions	**967,554**	**967,554**
Instruments issued by consolidated banking and financial subsidiaries of the Bank and held by third parties	–	
Total Adjustments to Tier 2	–	
Investment in own shares	–	
Others (specify)	–	
CET1 capital	**33,017,170**	**34,211,431**
Total Tier 1 capital	**33,017,170**	**34,211,431**
Total capital	**41,993,352**	**43,187,613**
Total Risk Weighted Assets (RWA)		
RWAs for Credit Risk	**237,481,831**	**237,671,154**
RWAs for Market Risk	**8,109,913**	**8,109,913**
RWAs for Operational Risk	**14,783,335**	**15,508,584**
CET1 Capital Ratio (including Capital Conservation Buffer, Countercyclical Capital Buffer and Surcharge on D-SIBs) (%)	**12.68%**	**13.09%**
of which: Capital Conservation Buffer (%)	**1.25%**	**1.25%**
of which: Countercyclical Buffer (%)	**N/A**	**N/A**
of which: Capital Surcharge on D-SIBs (%)	**N/A**	**N/A**
Total Tier 1 Capital Ratio (%)	**12.68%**	**13.09%**
Total Capital Ratio (including Capital Conservation Buffer, Countercyclical Capital Buffer and Surcharge on D-SIBs) (%)	**16.13%**	**16.53%**
of which: Capital Conservation Buffer (%)	**1.25%**	**1.25%**
of which: Countercyclical Buffer (%)	**N/A**	**N/A**
of which: Capital Surcharge on D-SIBs (%)	**N/A**	**N/A**

Credit Risk under Standardised Approach – Credit Risk Exposures and Credit Risk Mitigation (CRM) Effects

Asset Class	As at 31 December 2017 – Bank					
	Exposures before Credit Conversion Factor (CCF) and CRM		Exposures post CCF and CRM		RWA and RWA Density (%)	
	On-Balance Sheet Amount LKR 000	Off-Balance Sheet Amount LKR 000	On-Balance Sheet Amount LKR 000	Off-Balance Sheet Amount LKR 000	RWA LKR 000	RWA Density(ii)
Claims on Central Government and CBSL	**76,773,069**	**16,035,593**	**76,773,069**	**1,420,281**	**2,158,694**	**3%**
Claims on Foreign Sovereigns and their Central Banks	–	–	–	–	–	–
Claims on Public Sector Entities	**6,280,534**	–	**364,969**	–	**364,969**	**100%**
Claims on Official Entities and Multilateral Development Banks	–	–	–	–	–	–
Claims on Banks Exposures	**7,406,789**	**33,860,192**	**7,406,789**	**725,070**	**4,554,548**	**56%**
Claims on Financial Institutions	**9,079,267**	**562,500**	**9,079,267**	**375,000**	**5,382,553**	**57%**
Claims on Corporates	**95,723,730**	**55,980,424**	**90,556,225**	**25,793,187**	**113,273,818**	**97%**
Retail Claims	**45,068,598**	–	**36,436,649**	–	**32,730,202**	**90%**
Claims Secured by Residential Property	**9,171,660**	–	**9,147,320**	–	**7,547,539**	**83%**
Claims Secured by Commercial Real Estate	**43,913,872**	**585,219**	**43,913,872**	**585,219**	**44,499,092**	**100%**
Non-Performing Assets (NPAs) (i)	**2,804,072**	–	**2,804,072**	–	**3,689,728**	**132%**
Higher-risk Categories	**375,378**	–	**375,378**		**938,445**	**250%**
Cash Items and Other Assets	**21,303,137**	**4,826,702**	**21,160,735**	**4,826,702**	**22,358,057**	**86%**
Total	**317,900,106**	**111,850,630**	**298,018,345**	**33,725,459**	**237,481,831**	

Note:
(i) NPAs – As per Banking Act Directions on Classification of loans and advances, income recognition and provisioning.
(ii) RWA Density – Total RWA/Exposures post CCF and CRM.

Credit Risk under Standardised Approach – Credit Risk Exposures and Credit Risk Mitigation (CRM) Effects

Asset Class	As at 31 December 2017 – Group					
	Exposures before Credit Conversion Factor (CCF) and CRM		Exposures post CCF and CRM		RWA and RWA Density (%)	
	On-Balance Sheet Amount LKR 000	Off-Balance Sheet Amount LKR 000	On-Balance Sheet Amount LKR 000	Off-Balance Sheet Amount LKR 000	RWA LKR 000	RWA Density(ii)
Claims on Central Government and CBSL	**76,773,069**	**16,035,593**	**76,773,069**	**1,420,281**	**2,158,694**	**3%**
Claims on Foreign Sovereigns and their Central Banks	–	–	–	–	–	–
Claims on Public Sector Entities	**6,280,534**	–	**364,969**	–	**364,969**	**100%**
Claims on Official Entities and Multilateral Development Banks	–	–	–	–	–	–
Claims on Banks Exposures	**7,408,512**	**33,860,192**	**7,485,860**	**725,070**	**4,554,548**	**55%**
Claims on Financial Institutions	**9,079,267**	**562,500**	**9,079,267**	**375,000**	**5,382,553**	**57%**
Claims on Corporates	**95,723,730**	**55,980,424**	**90,556,225**	**25,793,187**	**113,273,818**	**97%**
Retail Claims	**45,068,598**	–	**36,436,649**	–	**32,411,557**	**89%**
Claims Secured by Residential Property	**9,171,660**	–	**9,147,320**	–	**7,547,539**	**83%**
Claims Secured by Commercial Real Estate	**43,913,872**	**585,219**	**43,913,872**	**585,219**	**44,499,092**	**100%**
Non-Performing Assets (NPAs)(i)	**2,804,072**	–	**2,804,072**	–	**3,689,728**	**132%**
Higher-risk Categories	**413,823**	–	**413,823**		**1,034,557**	**250%**
Cash Items and Other Assets	**21,719,944**	**4,826,702**	**21,577,542**	**4,826,702**	**22,754,099**	**86%**
Total	**318,357,081**	**111,850,630**	**298,552,668**	**33,655,685**	**237,671,154**	

Note:
(i) NPAs – As per Banking Act Directions on Classification of loans and advances, income recognition and provisioning.
(ii) RWA Density – Total RWA/Exposures post CCF and CRM.

Credit Risk under Standardised Approach: Exposures by Asset Classes and Risk Weights

Description	Amount (LKR 000) as at 31 December 2017 (Post CCF and CRM) – Bank							
Risk Weight Asset Classes	0%	20%	50%	75%	100%	150%	>150%	Total Credit Exposures Amount
Claims on Central Government and Central Bank of Sri Lanka	67,399,879	10,793,472	–	–	–	–	–	78,193,351
Claims on Foreign Sovereigns and their Central Banks	–	–	–	–	–	–	–	–
Claims on Public Sector Entities	–	–	–	–	364,969	–	–	364,969
Claims on Official Entities and Multilateral Development Banks	–	–	–	–	–	–	–	–
Claims on Banks Exposures	–	1,239,330	5,203,321	–	1,689,207		–	8,131,859
Claims on Financial Institutions	–	1,406,530	5,892,980	–	2,154,757	–	–	9,454,267
Claims on Corporates	–	2,245,892	2,557,762	–	111,545,759	–	–	116,349,412
Retail Claims	546,846	1,849,901	–	6,718,725	27,321,178	–	–	36,436,649
Claims Secured by Residential Property	–	–	3,199,563	–	5,947,757	–	–	9,147,320
Claims Secured by Commercial Real Estate	–	–	–	–	44,499,092	–	–	44,499,092
Non-Performing Assets (NPAs)	–	–	9,486	–	1,013,791	1,780,796	–	2,804,072
Higher-risk Categories	–	–	–	–	–	–	375,378	375,378
Cash Items and Other Assets	3,603,883	31,871	–	–	22,351,683	–	–	25,987,437
Total	71,550,607	17,566,996	16,863,112	6,718,725	216,888,193	1,780,796	375,378	331,743,806

Description	Amount (LKR' 000) as at 31 December 2017 (Post CCF and CRM) – Group							
Risk Weight Asset Classes	0%	20%	50%	75%	100%	150%	>150%	Total Credit Exposures Amount
Claims on Central Government and Central Bank of Sri Lanka	67,399,879	10,793,472	–	–	–	–	–	78,193,351
Claims on Foreign Sovereigns and their Central Banks	–	–	–	–	–	–	–	–
Claims on Public Sector Entities	–	–	–	–	364,969	–	–	364,969
Claims on Official Entities and Multilateral Development Banks	–	–	–	–	–	–	–	–
Claims on Banks Exposures	79,071	1,239,330	5,203,321	–	1,689,207		–	8,210,930
Claims on Financial Institutions	–	1,406,530	5,892,980	–	2,154,757	–	–	9,454,267
Claims on Corporates	–	2,245,892	2,557,762	–	111,545,759	–	–	116,349,412
Retail Claims	546,846	1,849,901	–	6,718,725	27,321,178	–	–	36,436,649
Claims Secured by Residential Property	–	–	3,199,563	–	5,947,757	–	–	9,147,320
Claims Secured by Commercial Real Estate	–	–	–	–	44,499,092	–	–	44,499,092
Non-Performing Assets (NPAs)	–	–	9,486	–	1,013,791	1,780,796	–	2,804,072
Higher-risk Categories	–	–	–	–	–	–	413,823	413,823
Cash Items and Other Assets	3,624,648	31,871	–	–	22,747,725	–	–	26,404,244
Total	71,650,443	17,566,996	16,863,112	6,718,725	217,284,235	1,780,796	365,177	332,278,130

Market Risk under Standardised Measurement Method

Item	31 December 2017 RWA Bank LKR 000	31 December 2017 RWA Group LKR 000
(a) RWA for Interest Rate Risk	912,365	912,365
General Interest Rate Risk	885,626	885,626
(i) Net Long or Short Position	885,626	885,626
(ii) Horizontal Disallowance	–	–
(iii) Vertical Disallowance	–	–
(iv) Options	–	–
Specific Interest Rate Risk	–	–
(b) RWA for Equity	12,567	12,567
(i) General Equity Risk	7,570	7,570
(ii) Specific Equity Risk	4,998	4,998
(c) RWA for Foreign Exchange & Gold	14,172	14,172
Capital Charge for Market Risk [(a) + (b) + (c)] * CAR	8,109,913	8,109,913

Operational Risk under Basic Indicator Approach – Bank

Business Lines		Capital charge factor (%)	Gross Income Year ended 31 December		
			2017 LKR 000	2016 LKR 000	2015 LKR 000
The basic indicator approach		**15**	**13,147,262**	11,308,687	8,806,555
Capital charges for operational risk (LKR 000)					
The basic indicator approach	**1,663,125**				
Risk weighted amount for operational risk (LKR 000)					
The basic indicator approach	**14,783,335**				

Operational Risk under Basic Indicator Approach – Group

Business Lines		Capital charge factor (%)	Gross Income Year ended 31 December		
			2017 LKR 000	2016 LKR 000	2015 LKR 000
The Basic Indicator Approach		15	**13,239,349**	11,564,991	10,089,973
Capital charges for operational risk (LKR 000)					
The basic indicator approach	1,744,716				
Risk weighted amount for operational risk (LKR 000)					
The basic indicator approach	15,508,584				

Differences between Accounting and Regulatory Scopes and Mapping of Financial Statement Categories with Regulatory Risk Categories – Bank only

	Amount (LKR 000) as at 31 December 2017					
Item	**Carrying values as reported in published financial statements**	**Carrying values under scope of regulatory reporting**	**Subject to credit risk framework**	**Subject to market risk framework**	**Not subject to capital requirements or subject to deduction from capital**	**Explanation for differences between accounting and regulatory reporting**
Assets						
Cash and cash equivalents	**4,106,225**	**4,108,401**	**4,108,401**	–		–
Balances with central banks	**10,557,688**	**10,557,688**	**10,557,688**	–		–
Placements with banks	**6,691,381**	**6,691,381**	**6,691,381**	–		–
Derivative financial instruments	**66,440**		–	–		Included under other asset in regulatory reporting
Other financial assets – held-for-trading	**310,922**	**36,974,546**	**36,907,117**	**67,429**		The difference is due to the Government and equity securities held for trading which are classified as AFS in published Financial Statements.
Loans and receivables to banks	**10,984,266**	–	–	–		Stated under held to maturity in regulatory reporting

Item	Carrying values as reported in published financial statements	Carrying values under scope of regulatory reporting	Subject to credit risk framework	Subject to market risk framework	Not subject to capital requirements or subject to deduction from capital	Explanation for differences between accounting and regulatory reporting
	Amount (LKR 000) as at 31 December 2017					
Loans and receivables to other customers	**213,675,866**	**213,027,200**	**196,846,026**	–	**19,953,307**	The impairment allowance for loans and advances on a collective and individual basis in accordance with LKAS 39 – Financial Instrument – Recognition and Measurement. The general and specific provisions are made in a accordance with Central Bank of Sri Lanka. The difference between the balance under SLFRS and previous GAAP.
Financial investments – available-for-sale (AFS)*	**56,866,054**	–	–	–		Classified into held to maturity and held for trading regulatory reporting
Financial investments – held-to-maturity*	**23,507,632**	**41,521,228**	**36,944,571**	–	**4,576,657**	The difference is due to the government and equity securities held for investment purposes which are classified as AFS in published financial statements.
Investments in subsidiaries	**167,036**	**202,305**	**202,305**	–		Investments in associates are included in regulatory reporting in addition to those in subsidiaries
Investments in associates and joint ventures	**790,270**	–	–	–		In regulatory reporting, the investments in joint ventures are stated under held to maturity
Property, plant and equipment	**1,273,250**	**1,273,250**		–		–
Goodwill and intangible assets	**498,084**	**498,084**	–	–	**498,084**	
Other assets	**3,612,228**	**4,391,724**	**4,518,513**	–		–
Total assets	**333,107,342**	**319,245,807**	**298,018,347**	**67,429**	**24,932,164**	–
Liabilities						
Due to banks	**9,640,735**	–	–	–	–	Included under Other Borrowings in regulatory reporting
Derivative financial instruments	**367,435**	–	–	–	–	Included under Other Liabilities in regulatory reporting
Due to other customers*	**193,307,534**	**186,692,330**	–	–	**186,692,330**	Interest payable on deposits are stated under Other Liabilities in regulatory reporting
Other borrowings*	**41,319,591**	**74,092,476**	–	–	**74,092,476**	Due to banks and Debt Securities Issued are included under this heading in regulatory reporting
Debt securities issued*	**24,443,767**	–	–	–	–	Included under Other Borrowings in regulatory reporting
Current tax liabilities	**633,636**	**503,367**	–	–	**503,367**	Taxes are computed based on different profits under each reporting method.
Deferred tax liabilities	**1,194,027**	**1,016,856**	–	–	**1,016,856**	Due to deferred tax adjustments on government securities classified as available for sale financial assets.
Other liabilities	**5,120,981**	**13,486,355**	–	–	**13,486,355**	Interest payable on Borrowing and deposits added to the Other Liabilities in regulatory reporting
Due to subsidiaries*	–	–	–	–	–	–
Subordinated term debts	**9,202,870**	**9,000,000**	–	–	**991,372**	Regulatory reporting reports only the principal amount
Total liabilities	**285,230,576**	**284,791,384**	–	–	**276,782,756**	–

Item	Carrying values as reported in published financial statements	Carrying values under scope of regulatory reporting	Subject to credit risk framework	Subject to market risk framework	Not subject to capital requirements or subject to deduction from capital	Explanation for differences between accounting and regulatory reporting
	Amount (LKR 000) as at 31 December 2017					
Off–balance sheet liabilities						
Guarantees	**12,480,687**	**12,480,687**	**12,480,687**	–		–
Performance bonds	**4,090,585**	**4,090,585**	**4,090,585**	–		–
Letters of credit and acceptances	**15,098,107**	**15,098,107**	**15,098,107**	–		–
Other contingent items (bills on collection and capital expenditure approved by the board)	**2,305,466**	**2,305,466**		–	**2,305,466**	–
Undrawn loan commitments	**62,852,575**	**62,852,575**	**62,852,575**	–		–
Other commitments (FX commitments)	**38,743,903**	**38,743,903**	**38,743,903**	–		–
Total off–balance sheet liabilities	**135,571,324**	**135,571,324**	**133,265,858**	–	**2,305,466**	–
Shareholders' equity						
Equity capital (stated capital)/ assigned capital of which amount eligible for CET1 of which amount eligible for AT1	**4,715,814**	**4,715,814**	–	–		–
Retained earnings	**13,858,152**	**13,847,980**	–			Due to differences which arise in profits computed in previous GAAP and SLFRSs
Accumulated other comprehensive income	**13,298,686**	–	–	–	–	Accumulated other comprehensive income is only applicable in published Financial Statements
Other reserves	**16,004,114**	**15,890,629**	–	–	**15,784,114**	Due to differences which arise in profits computed in previous GAAP and SLFRSs
Total shareholders' equity	**47,876,766**	**34,454,475**	–	–	**15,784,114**	–

Note:
** Regulatory reporting to Central Bank of Sri Lanka is based on previous GAAP where as published financial statements are based on Sri Lanka Financial Reporting Standards (SLFRSs).*

** The effective interest rate (EIR) adjustments required by LKAS 39 on these financial instruments are adjusted in published financial statements.*

Main Features of Regulatory Capital Instruments

Description of the Capital Instrument (Bank Only)	Stated Capital	Subordinated Term-debt (2015)	Subordinated Term-debt (2016 – Type A)	Subordinated Term-debt (2016 – Type B)
Issuer	DFCC Bank PLC	DFCC Bank PLC	DFCC Bank PLC	DFCC Bank PLC
Unique Identifier (e.g., ISIN or Bloomberg Identifier for Private Placement)	LK0055N00000	C2306	C 2366	C-2367
Governing Law(s) of the Instrument	Companies Act, No. 07 of 2007, Colombo Stock Exchange Regulations	Securities and Exchange Commission Act No. 36 of 1987 (as amended), Colombo Stock Exchange Regulations		
Original Date of Issuance	May 1956 to November 2010	10 June 2015	9 November 2016	9 November 2016
Par Value of Instrument (LKR)	10	100	100	100
Perpetual or Dated	Perpetual	Dated	Dated	Dated
Original Maturity Date, if Applicable	N/A	10/6/2020	9/11/2021	9/11/2023
Amount Recognised in Regulatory Capital (in LKR '000 as at the Reporting Date)	4,715,814	1,200,000	765,488	6,043,140
Accounting Classification (Equity/Liability)	Equity	Liability	Liability	Liability
Issuer Call subject to Prior Supervisory Approval				
Optional Call Date, Contingent Call Dates and Redemption Amount (LKR '000)	N/A	N/A	N/A	N/A
Subsequent Call Dates, if Applicable	N/A	N/A	N/A	N/A
Coupons/Dividends				
Fixed or Floating Dividend/Coupon	Floating dividend	Fixed coupon	Fixed coupon	Fixed coupon
Coupon Rate and any Related Index (%)	N/A	9.4	12.15	12.75
Non-Cumulative or Cumulative	Non-Cumulative	Non-Cumulative	Non-Cumulative	Non-Cumulative
Convertible or Non-Convertible	Non-convertible	Non-convertible	Non-convertible	Non-convertible
If Convertible, Conversion Trigger (s)	N/A	N/A	N/A	N/A
If Convertible, Fully or Partially	N/A	N/A	N/A	N/A
If Convertible, Mandatory or Optional	N/A	N/A	N/A	N/A
If Convertible, Conversion Rate	N/A	N/A	N/A	N/A

N/A – Not applicable

Ten Year Summary

LKR million	Based on previous GAAP			Based on current SLFRS						
	For the year ended 31 March							For the 9 months ended 31 December	For the year ended 31 December	
	2009	2010	2011	2012	2013	2014	2015	2015	2016	**2017**
Bank										
Operating Results										
Total income	9,888	8,843	14,191	7,652	10,433	10,481	10,394	10,036	26,754	**35,942**
Profit before income tax	2,006	2,402	7,876	2,883	3,492	3,211	3,771	1,589	4,414	**5,792**
Income tax expense	646	689	739	430	570	623	531	521	1,125	**1,377**
Profit after tax	1,360	1,713	7,137	2,453	2,921	2,587	3,240	1,068	3,289	**4,415**
Statement of Financial Position										
Assets										
Cash and short-term funds	8,415	10,472	11,991	3,646	7,103	4,245	2,296	9,859	13,745	**21,355**
Loans to and receivables from banks and other customers	40,247	36,681	39,344	54,982	60,668	62,575	73,933	164,920	198,085	**224,660**
Financial investments	1,918	1,999	4,032	16,277	19,298	25,609	29,909	66,861	72,461	**80,374**
Investment in associate, joint venture and subsidiary companies	6,064	5,845	3,132	4,451	4,446	6,659	6,648	823	902	**957**
Other assets	1,841	1,419	1,427	1,841	1,645	1,853	1,826	3,688	4,868	**5,761**
Total assets	58,485	56,416	59,926	81,197	93,160	100,941	114,612	246,151	290,061	**333,107**
Liabilities										
Due to other customers	5,308	5,124	3,688	12,445	15,548	16,630	22,485	110,891	140,514	**193,308**
Other borrowings	36,710	33,530	32,261	36,489	41,605	45,262	46,346	87,379	97,240	**84,607**
Other liabilities	1,976	2,039	3,758	1,010	1,223	1,639	1,686	5,062	6,457	**7,316**
Equity	14,491	15,723	20,219	31,253	34,784	37,410	44,095	42,819	45,850	**47,877**
Total equity and liabilities	58,485	56,416	59,926	81,197	93,160	100,941	114,612	246,151	290,061	**333,107**
Return on equity (%)**	9.6	11.3	39.7	11.7	12.9	10.6	12.8	5.0	10.99	**13.4**
Return on total assets (%)**	2.2	3.0	12.3	3.7	3.8	3.0	3.5	1.0	1.30	**1.48**
Earnings per share (LKR)*	5.17	6.48	26.95	9.25	11.02	9.76	12.22	4.03	12.41	**16.65**
Market value per share (LKR)*	33.78	90.23	171.8	112.6	131.1	143.9	202.8	168.1	122.50	**124.00**
Price earnings ratio (times)*	6.5	13.9	6.4	12.2	11.9	14.7	16.6	41.7	9.87	**7.45**
Earnings yield (%)*	15.4	7.2	15.6	8.2	8.4	6.8	6.0	2.4	10.13	**13.43**
Dividend per share (LKR)	5.00	6.00	10.00	4.00	5.00	5.50	6.00	2.5	4.5	**5.0**
Dividend cover (times)	2.1	2.2	2.7	3.1	2.8	2.0	2.2	0.7	4.96	**3.70**
Gross dividend (LKR million)	653.7	794.3	2,649	795	1,060	1,325	1,458	1,591	663	**1,193**
Liquid assets to liabilities (as specified in the Banking Act No. 30 of 1998) (%)	145	214	295	52	53	77	48	22	27	**27**
No. of employees	419	427	451	466	461	477	495	1,445	1,642	**1,770**

** Adjusted for bonus issue*

*** After eliminating fair value reserve*

Corporate Information

Name of Company

DFCC Bank PLC

Legal Form

A quoted public company with limited liability incorporated by DFCC Bank Act No. 35 of 1955 and with the enactment of the DFCC Bank (Repeal and Consequential Provisions) Act No. 39 of 2014, incorporated under the Companies

Act No. 07 of 2007 with the name "DFCC Bank PLC" with effect from 6 January 2015.

A licensed commercial bank under the Banking Act, No. 30 of 1988.

Company Registration Number:

PQ233

Credit Rating

AA- (lka) credit rating from Fitch Ratings Lanka Limited.

Annual General Meeting (AGM)

The AGM will be held at the Cinnamon Lakeside Colombo, Sir Chittampalam A Gardiner Mawatha, Colombo 2, on 28 March 2018.

Details of the business of the meeting and other information are contained in the booklet enclosed with this Annual Report.

For any clarification on this Report please write to:

The Company Secretary
DFCC Bank PLC
No. 73/5, Galle Road,
Colombo 03, Sri Lanka or
E-mail to: info@dfccbank.com

Company Secretary

Ms A Withana

Auditors

KPMG
Chartered Accountants

VAT Registration No.

409000088-7000

Registered Office

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Notes

Notes

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