



Merchant Bank of Sri Lanka & Finance PLC

FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2023

Fitch - BBB+(Ika)
Co. Reg. No. PQ 10



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தேசிய கணக்காய்வு அலுவலகம்
NATIONAL AUDIT OFFICE



27 March 2024

Chairman
Merchant Bank of Sri Lanka and Finance PLC
Report of the Auditor General on the Financial Statements and Other Legal and Regulatory Requirements of the Merchant Bank of Sri Lanka and Finance PLC and its subsidiary for the year ended 31 December 2023 in terms of Section 12 of the National Audit Act, No. 19 of 2018.

1. Financial Statements

1.1 Opinion

The audit of the Financial Statements of the Merchant Bank of Sri Lanka and Finance PLC (the "Company") and the Consolidated Financial Statements of the Company and its subsidiary (the "Group") for the year ended 31 December 2023 comprising the statement of financial position as at 31 December 2023 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the Financial Statements, including material accounting policy information, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018. My report to Parliament in pursuance of provisions in Article 154 (6) of the Constitution will be tabled in due course. To carry out this audit I was assisted by a firm of Chartered Accountants in public practice.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Company and the Group as at 31 December 2023 and of their financial performance and their cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

1.3 Key Audit Matters

Key audit matters are those matters that, in my professional judgment, were of most significance in my audit of the financial statements of the current period. These matters were addressed in the context of the audit of the financial statements as a whole, and in forming my opinion thereon, and I do not provide a separate opinion on these matters. For each matter below, my description of how my audit addressed the matter is provided in that context.

I have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the financial statements section of my report, including in relation to these matters. Accordingly, my audit included the performance of procedures designed to respond to my assessment of the risks of material misstatement of the financial statements. The results of my audit procedures, including the procedures performed to address the matters below, provide the basis for my audit opinion on the accompanying financial statements.

| Key audit matter | How my audit addressed the key audit matter |
|---|---|
| Allowance for Impairment Losses on Loans & Receivables at Amortised Cost Allowance for impairment losses on loans & receivables at amortised cost as stated in Note 12 & 23, respectively, is determined by management based on the accounting policies described in Note 3.5.11. | In addressing the adequacy of the allowance for impairment losses on loans & receivables at amortised cost, my audit procedures included the following key procedures: <ul style="list-style-type: none">I assessed the alignment of the Company's allowance for impairment loss computations and underlying methodology including responses to current economic conditions with its accounting policies, based on the best available information up to the date of my report.I evaluated the design, implementation, and operating effectiveness of controls over estimation of allowance for impairment losses, which included assessing the level of oversight, review and approval of allowance for impairment losses, policies and procedures by the Board and management.I checked the completeness, accuracy and reasonableness of the underlying data used in the allowance for impairment loss computations by agreeing details to relevant source documents and accounting records of the Company.I evaluated the reasonableness of credit quality assessments and related stage classifications.In addition to the above, the following procedures were performed:<ul style="list-style-type: none">For loans and receivables assessed on an individual basis for impairment:<ul style="list-style-type: none">I checked the arithmetical accuracy of the underlying individual impairment calculations.I evaluated the reasonableness of key inputs used in the allowance for impairment losses made with particular focus on current economic conditions. Such evaluations were carried out considering the value and timing of cash flow forecasts particularly relating to elevated risk industries and status of recovery action of the collateral.For loans & receivables assessed on a collective basis for impairment:<ul style="list-style-type: none">I tested the key inputs and the calculations used in the allowance for impairment losses.I assessed the reasonableness of judgements, assumptions and estimates used by the Management in the underlying methodology and the management overlays. My testing included evaluating the reasonableness of forward-looking information used, economic scenarios considered, and probability weighting assigned to each of those scenarios.I assessed the adequacy of the related financial statement disclosures set out in notes 3.5.11, 12.23 and 47.2. |
| This was a key audit matter due to <ul style="list-style-type: none">the involvement of significant management judgements, assumptions and level of estimation uncertainty associated in estimating management expectation of future cash flows to recover such loans & receivables; andthe materiality of the reported amount of allowance for impairment losses and use of complex calculations in its determination. Key areas of significant judgements, assumptions and estimates used by management in the assessment of the allowance for impairment losses on loans & receivables at amortised cost included: assumed future occurrences of events and conditions relating to the forward-looking macroeconomic scenarios and their associated weightages, which are subject to inherently heightened levels of estimation uncertainty. | |
| Information Technology (IT) systems related internal controls over financial reporting Company's financial reporting process is significantly reliant on multiple IT systems with automated processes and internal controls. Further, key financial statement disclosures are prepared using data and reports generated by IT systems, that are compiled and formulated with the use of spreadsheets. Accordingly, IT systems related internal controls over financial reporting were considered a key audit matter | My audit procedures included the following key procedures: <ul style="list-style-type: none">I obtained an understanding of the internal control environment of the processes and test checked relevant controls relating to financial reporting and related disclosures.I involved our internal specialized resources and;I identified, evaluated and tested the design and operating effectiveness of IT systems related internal controls, including those related to user access and change management, andI obtained a high-level understanding of the cybersecurity risks affecting the Company and the actions taken to address these risks primarily through inquiry.I tested source data of the reports used to generate disclosures for accuracy and completeness, including review of the general ledger reconciliations. |

1.4 Other information included in the Company's 2023 Annual Report

The other information comprises the information included in the Company's 2023 Annual Report, but does not include the financial statements and my auditor's report thereon, which is expected to be made available to me after the date of this auditor's report. Management is responsible for the other information. My opinion on the financial statements does not cover the other information and I do not express any form of assurance conclusion thereon.

In connection with my audit of the financial statements, my responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit or otherwise appears to be materially misstated.

When I read the Company's 2023 Annual Report, if I conclude that there are material misstatements therein, I am required to communicate that matter to those charged with governance for correction. If further material uncorrected misstatements are existed those will be included in my report to Parliament in pursuance of provisions in Article 154 (6) of the Constitution that will be tabled in due course.

1.5 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of Financial Statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of Financial Statements that are free from material misstatement, whether due to fraud or error.

In preparing the Financial Statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process. As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company and the Group is required to maintain proper books and records of all their income, expenditure, assets and liabilities, to enable annual and periodic Financial Statements to be prepared of the Company and the Group.

1.6 Auditor's Responsibilities for the Audit of the Financial Statements

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

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control of the Company and the Group.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the Financial Statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion.

2. Report on Other Legal and Regulatory Requirements

- National Audit Act, No. 19 of 2018 and Companies Act, No. 7 of 2007 include specific provisions for following requirements.
 - I have obtained all the information and explanation that required for the audit and as far as appears from my examination, proper accounting records have been kept by the Company as per the requirement of section 163 (2) (d) of the Companies Act, No. 7 of 2007 and the section 12 (a) of National Audit Act, No. 19 of 2018.
 - The financial statements of the Company comply with the requirement of section 151 of the Companies Act, No. 07 of 2007.
 - The financial statements presented is consistent with the preceding year as per the requirement of section 6 (1) (d) (ii) of the National Audit Act, No. 19 of 2018.
 - The financial statements presented includes all the recommendations made by me in the previous year as per the requirement of section 6 (1) (d) (iv) of the National Audit Act, No. 19 of 2018.
- Based on the procedures performed and evidence obtained were limited to matters that are material, nothing has come to my attention;
 - to state that any member of the governing body of the Company has any direct or indirect interest in any contract entered into by the Company which are out of the normal course of business as per the requirement of section 12 (d) of the National Audit Act, No. 19 of 2018.
 - to state that the Company has not complied with any applicable written law, general and special directions issued by the governing body of the Company as per the requirement of the section 12 (f) of the National Audit Act, No. 19 of 2018 ;
 - to state that the Company has not performed according to its powers, functions and duties as per the requirement of section 12 (g) of the National Audit Act, No. 19 of 2018.
 - to state that the resources of the Company had not been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws as per the requirement of section 12 (h) of the National Audit Act, No. 19 of 2018.

W.P.C. Wickramaratne
Auditor General

Merchant Bank of Sri Lanka & Finance PLC
(Subsidiary of Bank of Ceylon)
BOC Merchant Tower,
No. 28, St. Michael's Road, Colombo 03, Sri Lanka.
Tel : 011 4 711 711, Fax: 011 4 711 765
E-mail : mbslbank@mbslbank.com
Web Site : www.mbslbank.com

| STATEMENT OF PROFIT OR LOSS | 2023 Rs. 000 | 2022 Rs. 000 |
|---|--------------------|--------------------|
| Income | 7,478,049 | 6,542,593 |
| Interest and similar income | 6,559,123 | 6,451,083 |
| Interest and similar expenses | (4,918,658) | (4,695,684) |
| Net interest income | 1,640,465 | 1,755,399 |
| Fee and commission income | 123,292 | 129,157 |
| Fee and commission expenses | (16,757) | (19,205) |
| Net fee and commission income | 106,535 | 109,952 |
| Net trading income | 120,243 | 3,658 |
| Net gain/(loss) on financial instruments at fair value through profit or loss | 559,224 | (132,131) |
| Other operating income | 116,167 | 90,826 |
| Total operating income | 2,542,634 | 1,827,704 |
| Allowance for impairment losses charge for loans and other assets | 25,094 | 16,504 |
| Net operating income | 2,567,728 | 1,844,208 |
| Personnel expenses | (1,289,690) | (1,333,268) |
| Depreciation and amortisation | (272,869) | (265,420) |
| Other operating expenses | (739,416) | (660,683) |
| Total operating expenses | (2,301,975) | (2,259,371) |
| Operating profit/(loss) before VAT on financial services and impairment of investment in group companies | 265,753 | (415,163) |
| Impairment reversal/(charge) of investment in subsidiary | 95,065 | (113,773) |
| Profit/(loss) from operations after impairment of investment in group companies | 360,818 | (528,936) |
| Taxes on financial services | (292,911) | (127,978) |
| Profit/(loss) before income tax | 67,907 | (656,914) |
| Income tax (expense)/reversal | (47,019) | 161,306 |
| Profit/(loss) for the year | 20,888 | (495,608) |
| Earnings per share: | | |
| Basic/diluted earnings/(loss) per share: | 0.04 | (0.94) |

| STATEMENT OF COMPREHENSIVE INCOME | 2023 Rs. 000 | 2022 Rs. 000 |
|---|-----------------|------------------|
| Profit/(loss) for the year | 20,888 | (495,608) |
| Other comprehensive income/(expenses) | | |
| Other comprehensive income to be reclassified to profit or loss in subsequent periods (net of tax): | | |
| Gains/(losses) on re-measuring financial investments at fair value through other comprehensive income | (1,515) | (10,735) |
| Net other comprehensive income/(expenses) to be reclassified to profit or loss in subsequent periods | (1,515) | (10,735) |
| Other comprehensive income not to be reclassified to profit or loss in subsequent periods (net of tax): | | |
| Actuarial gains/(losses) on defined benefit plans | (63,207) | 47,045 |
| Deferred tax effect relating to components of other comprehensive income | 18,962 | (14,113) |
| Net other comprehensive income/(expenses) not to be reclassified to profit or loss in subsequent periods | (44,245) | 32,932 |
| Other comprehensive income/(expenses) for the year, net of tax | (45,760) | 22,197 |
| Total comprehensive income/(expenses) for the year, net of tax | (24,872) | (473,411) |

| STATEMENT OF FINANCIAL POSITION | 2023 Rs. 000 | 2022 Rs. 000 |
|--|-------------------|-------------------|
| Assets | | |
| Cash and cash equivalents | 720,397 | 748,724 |
| Placements with banks & financial institutions | 574,588 | 103,682 |
| Financial investments at fair value through profit or loss | 8,161,368 | 287,510 |
| Loans & receivables at amortised cost | 19,054,715 | 24,423,300 |
| Financial investments at fair value through other comprehensive income | 14,348 | 15,863 |
| Financial investments at amortised cost | 3,727,940 | 4,307,394 |
| Real estate stock | 58,158 | 96,937 |
| Investment in associate | 81,084 | 81,084 |
| Investment in subsidiary | 352,696 | 257,631 |
| Investment properties | 95,446 | 104,798 |
| Property, equipment and right-of-use assets | 585,436 | 504,669 |
| Intangible assets | 67,117 | 103,208 |
| Deferred tax assets | 54,951 | 33,824 |
| Other assets | 150,878 | 163,157 |
| Total assets | 33,699,122 | 31,231,781 |
| Liabilities | | |
| Due to banks | 2,599,970 | 2,925,953 |
| Due to customers at amortised cost | 25,444,119 | 23,524,609 |
| Debt issued and borrowed funds at amortised cost | 741,030 | 69,082 |
| Current tax liabilities | 30,055 | 49,029 |
| Other liabilities | 858,908 | 686,361 |
| Retirement benefits obligations | 354,368 | 281,203 |
| Total liabilities | 30,028,450 | 27,536,237 |
| Equity | | |
| Stated capital | 4,276,448 | 4,276,448 |
| Statutory reserves | 344,174 | 339,996 |
| Retained earnings | (1,289,648) | (944,964) |
| RLA reserve | 371,590 | 54,441 |
| OCI reserve | (31,892) | (30,377) |
| Total equity | 3,670,672 | 3,695,544 |
| Total liabilities and equity | 33,699,122 | 31,231,781 |
| Commitments and contingent liabilities | 42,093 | 103,938 |
| Net assets value per share (Rs.) | 7.00 | 7.05 |

| SELECTED PERFORMANCE INDICATORS | As at 31/12/2023 (Unaudited) | As at 31/12/2022 (Unaudited) |
|---|------------------------------------|------------------------------------|
| Regulatory capital adequacy | | |
| Core capital (tier 1 capital), Rs. '000 | 2,950,935 | 2,973,001 |
| Total capital base, Rs. '000 | 3,634,681 | 3,151,598 |
| Core capital adequacy ratio, as % of risk weighted assets (minimum requirement, 8.5%) | 13.60% | 11.33% |
| Total capital adequacy ratio, as % of risk weighted assets (minimum requirement, 12.5%) | 16.75% | 12.01% |
| Capital funds to deposit liabilities ratio (minimum requirement, 10%) | 15.75% | 15.89% |
| Assets quality (quality of loan portfolio) | | |
| Gross non-performing accommodations, Rs.'000 | 4,579,316 | 5,161,299 |
| Gross non-performing accommodations ratio, % | 21.06% | 17.77% |
| Net non performing accommodations ratio, % | 7.12% | 8.14% |
| Profitability(%) | | |
| Interest margin | 5.55% | 5.85% |
| Return on assets (before tax) | 0.21% | -2.01% |
| Return on equity (after tax) | 0.57% | -12.60% |
| Regulatory liquidity (Rs. '000) | | |
| Required minimum amount of liquid assets | 2,859,509 | 2,636,887 |
| Available amount of liquid assets | 3,257,794 | 3,485,014 |
| Required minimum amount of government securities | 2,086,865 | 1,894,394 |
| Available amount of government securities | 2,979,348 | 2,992,197 |
| Memorandum information | | |
| Number of employees | 785 | 893 |
| Number of branches | 48 | 48 |

Certification;
We, the undersigned, being the Chief Financial Officer and the Chief Executive Officer of Merchant Bank of Sri Lanka & Finance PLC certify jointly that:
(a) The above statements have been prepared in compliance with the format and definitions prescribed by the Central Bank of Sri Lanka;
(b) The information contained in these statements have been extracted from audited financial statements of the Licensed Finance Company unless indicated as "Unaudited".

(Sgd.)
W K C S Vithana
Chief Financial Officer
25/03/2024

(Sgd.)
H K D W M D K Hapuhinna
Chief Executive Officer
25/03/2024