pru•dent

adjective

1. wise or judicious in practical affairs; sagacious; discreet or circumspect; sober.
2. careful in providing for the future; provident: *a prudent decision.*

Synonyms

1. sensible. 2. economical, thrifty, frugal.

Mercantile Investments and Finance PLC

Integrated Annual Report 2016/17

pru • dent

adjective

1. wise or judicious in practical affairs; sagacious; discreet or circumspect; sober.
2. careful in providing for the future; provident: *a prudent decision.*

Synonyms

1. sensible. 2. economical, thrifty, frugal.

When you think of Mercantile Investments, the words that come to mind are solid, successful, experienced…and prudent. Not for us the reckless risks of unguarded ambition, the desire to always be first nor the need to be constantly heard. Since our decisions are taken with care, we have continued to trust in our judgement and take the safe path, secure in the knowledge that our vision is clear and our business proposition progressive and strong.

We are proud to be known as a conservative company with old fashioned values, for our management policies have made us a model of stability in the fast paced and constantly changing world of business and finance today. We believe in serving our diverse stakeholders with real and sustainable value through the prudent policies we follow; the promise of triple bottom line excellence that people can count on, both now and in the years that lie ahead.

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Integrated Annual Report 2016/17
Visit MI Website

http://mi.com. lk/value-creation/annual-report-201617/

Overview

ca•pa•ble

adjective

1. having power and ability

2. efficient; competent

Synonyms

1. able, effective 2. accomplished, adept

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Overview

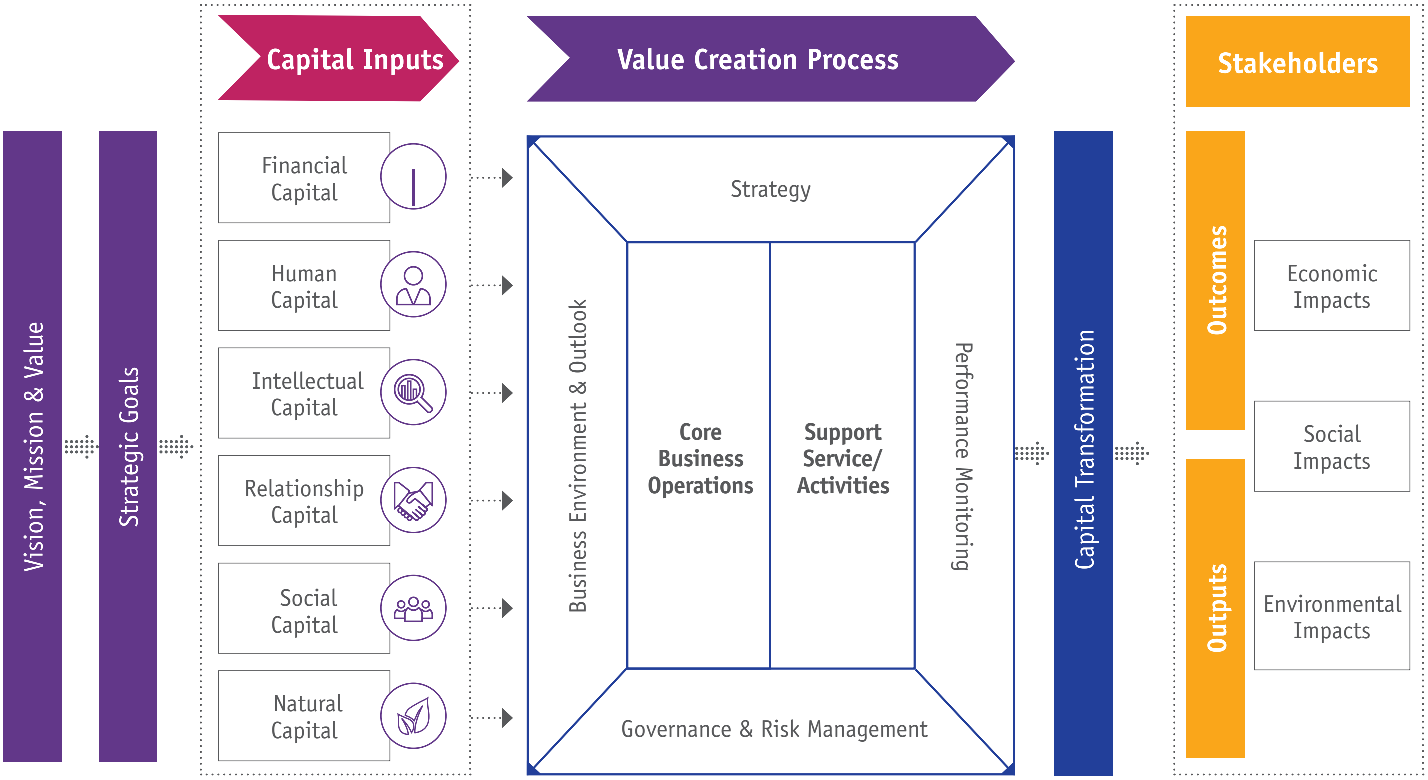
About the Report

We take pride in presenting our Integrated Annual Report which has been prepared in accordance with the International Integrated Reporting framework of 2013, issued by the International Integrated Reporting Council (IIRC), for the fourth consecutive year. The report articulates Mercantile Investments and Finance PLC's (MI's) business model and performance over time, emphasising primarily this year's progress, by capturing the essence in order that our investors and other key stakeholders can make a fair assessment of our efforts. We explain the progress in terms of our business model, the six types of capital employed in value generation which includes sustainability impacts with comparatives and forecasts where applicable. As an organisation that excels in financial reporting, we have continued to uphold greater corporate transparency during our fifty year business journey, which has led us to be better integrated thinkers in generating the required value to our key stakeholders.

Our Integrated Business Model

At Mercantile Investments and Finance PLC, we are committed in our visionary aspirations of excelling in our sphere of providing access to financial capital, returns commensurate with risks, and inclusivity as a Company engaged in the provision of financial services, and aspire to contributing to a more sustainable economy, society and an environment that is well protected. In creating value, we rely on the precepts of sustainability and the Company follows an effective business model that aligns MI's business operation to its well defined corporate strategy over the long term. At the heart of our business model is the primary goal of sustainable wealth creation for our investors and key stakeholders over the long term. Our business model is centred around a value generating process which subjects six capital inputs through a streamlined process of value creation, resulting in output capitals and sustainable outcomes of significance to our key stakeholders, as depicted in the diagram below. The past 50 years have given us the opportunity and the time to gain a wealth of experience, acquire and fine tune our skill sets and focus our attention towards integrated thinking. Our deep understanding of the market conditions and customer behaviour over 50 years of being a going concern, have led us to master the art of value creation, by using the six forms of capital, and subjecting them through a streamlined core business process and

MI's Integrated Business Model



Refer pages 38 to 39 for the quick reference of the Annual Report disclosure to the integrated business model.

Overview

various support activities associated with our business, to derive sustainable wealth for our key stakeholders. The six forms of capital used in the wealth creation process are, financial capital, relationship capital, human capital, intellectual capital, social and natural capital. Our Brand which is known for its financial strength and stability has been the foundation upon which we have built our integrated business model.

As part of the capital management and value creation process that we engage in, we continuously scan, evaluate and analyse the business environment, develop suitable strategies that take a long term view in setting our goals, and ensure there is continuous performance monitoring at various levels to ensure we achieve the targets we set for ourselves. We understand the different interlinks among the six capital elements, to finally generate the required financial returns for our investors whilst ensuring we remain a socially responsible enterprise that is protective of the environment. In managing risk and potential negative outcomes, we adhere to effective governance and risk management frameworks, that encompass high level risk management techniques and a strong control environment supported by sound corporate policies, procedures and practices and continuous assurance and review, best suited for the finance industry. Moreover, the success of MI's business revolves around its people who manage it and make the organisation's mission and objectives a reality. Whilst being fortunate to have a strong human capital base of over 800 staff members, we also possess the required intellectual capital, the know-how, and brand equity while being on the verge of acquiring an advanced Information Communication Technology (ICT), to take our prestigious organisation to greater heights.

☑ *G4-17*

Reporting Parameters

Scope of Report /Reporting Boundary

The commentary provided in this Report refers to activities of Mercantile Investments and Finance PLC, within the geographical boundaries of Sri Lanka, as MI does not operate any branches or subsidiaries, in other countries. The report discloses corporate strategy, analysis, discussion on operational and financial performance and initiatives and impacts pertaining to sustainability relevant to the Company for the financial year ended 31 March 2017, together with comparative information. There are no holding and subsidiary companies in MI's structure, however, it does include an associate company, Nuwara Eliya Hotels Company PLC in which MI has a 26.12% shareholding. The Company notes that any impact arising from activities of its associate Nuwara Eliya Hotels Company PLC, is insignificant for purpose of detailed reporting. However, the audited Financial Statements appearing under the section titled Financial Reports, disclose the consolidated position inclusive of MI's associate company, Nuwara Eliya Hotels Company PLC, which has been incorporated to the Financial Statements in accordance with LKAS/SLFRS requirements. Unless otherwise stated, information both financial and non-financial in nature contained in this Report has been either extracted from the Financial Statements of the Company or through internally maintained records.

Regulations Complied With

Sri Lanka Accounting Standards (LKAS/SLFRS)

The Audited Financial Statements contained in this Report have been prepared and presented in accordance with requirements of the Sri Lanka Accounting Standards (LKAS) and Sri Lanka Financial Reporting Standards (SLFRS) issued by the Institute of Chartered Accountants of Sri Lanka. The financial information provided in the Management Discussion and Analysis, corresponds to the LKAS/SLFRS based Audited Financial Statement balances where applicable.

Other Reporting Regulations and Recommended Disclosures

Disclosures contained in this Report are complaint with reporting requirements stemming from other key regulations listed below.

The Companies Act No. 07 of 2007, provisions stipulated by the Central Bank of Sri Lanka, including the Finance Business Act No. 42 of 2011 and the Rules of Disclosure of the Colombo Stock Exchange and Listing Requirements of the Securities and Exchange Commission (SEC).

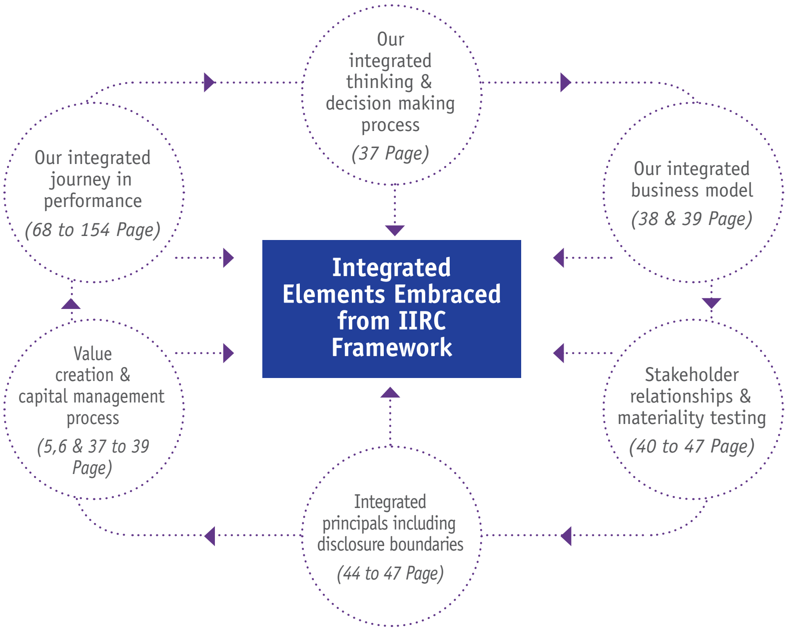
The Governance Report on pages 182 to 242 of this Report discusses in detail our governance structure and related compliance, along with a comprehensive disclosure covering requirements of the Code of Best Practice on Corporate Governance, issued jointly by the Institute of Chartered Accountants of Sri Lanka and the Securities and Exchange Commission of Sri Lanka (Release - 2013), the Finance Companies (Corporate Governance) Direction No. 03 of 2008 and related amendments issued by the Central Bank of Sri Lanka.

Frameworks Adopted

International Integrated Reporting Framework

In preparing the Integrated Annual Report, we have drawn reference to the International Integrated Reporting framework of 2013 (www.theiirc.org), and accordingly, in describing our unique value creation process, we have followed the related concepts, principles and guidance for the effective communication of our integrated thinking, decision making and capital management process.

Integrated Elements Embraced from IIRC Framework



☑ G4-32,33

Global Reporting Initiative (GRI) Sustainability Reporting Framework

"G4 Comprehensive Reporting"

To better articulate our sustainability efforts, this is the third consecutive year in which we have adopted the GRI's G4 reporting framework and the second consecutive year in which we have complied with the standard disclosure of "In Accordance - Comprehensive Reporting", together with the sector specific disclosures. The reporting approach taken including our key stakeholder engagement process, materiality testing and topic selecting process are explained on pages 40 to 47 under "Deciding on the Report Content". To ensure effective communication of our sustainability impacts for the concluded financial year 2016/17, the following broader topics/aspects have been covered comprehensively, in keeping to the framework.

General Standard Disclosures	**"In Accordance – Comprehensive" Reporting given**
Strategy and Analysis	G4-1 and G4-2
Organisational Profile	G4-3 to G4-16
Identified Material Aspects and Boundaries	G4-17 to G4-23
Stakeholder Engagement	G4-24 to G4-27
Report Profile	G4-28 to G4-33
Governance	G4-34 to G4-55
Ethics and Integrity	G4-56 to G4-58
General Standard Disclosures for Financial Services Sector	None to be reported

Specific Standard Disclosure	**"In Accordance – Comprehensive" Reporting given**
Generic Standard Disclosures on Management Approach	Disclosures given for material aspects selected
Indicators	All indicators given related to each identified material aspect
Specific Standard Disclosures for Financial Services Sector	Sector specific requirements have been given for all material aspects selected

Overview

Other Key Considerations

Assurance Reports

Subject matter for which External Assurance obtained	Output from assurance	External assurance obtained from	Page No.
Financial :			
1. Annual Financial Statements	External Audit Report	Messrs.' BDO Partners, Chartered Accountants	288
Sustainability :			
2. 2.a Sustainability Disclosures	Assurance Report	Messrs.' BDO Partners, Chartered Accountants	170
2.b Greenhouse Gas Emission Verification	Assurance Report	Sri Lanka Climate Fund (Pvt) Ltd	141
Governance :			
3. Compliance Status to Corporate Governance Direction issued by CBSL	Reference to Agreed Upon Procedures	Messrs.' BDO Partners, Chartered Accountants	242
Risk Controls :			
4. Directors' Statement on Internal Controls	Assurance Report	Messrs.' BDO Partners, Chartered Accountants	287

The external assurance providers operate independently in carrying out their reviews. The Board of Directors of MI along with the Corporate Management have no direct dealings or have any links with the external assurance providers.

☑ *G4-23*

Material Changes since Last Reporting Date

No significant changes to the scope, boundary and reporting basis have been noted since the last reporting date of 31st March 2016.

Availability of the Annual Report

Copies of the Annual Report have been sent to all shareholders, prior to holding the Annual General Meeting, in accordance with the prescribed period of notice. The Report has been also made available on MI's corporate website www.mi.com.lk and the CSE website www.cse.lk. (The Report can be viewed by referring to MI stock code "MERC").

☑ *G4-31*

Contact and Address:

Contact point for comments or queries with regard to this Annual Report should be sent via mail or e-mail to;

The General Manager Finance,
Mercantile Investments and Finance PLC,
236, Galle Road,
Colombo 03.
E-mail : accounts@mi.com.lk

☑ *G4-48*

Responsibility for the Integrity of the Integrated Report and Sustainability Reporting

I acknowledge the integrity of the disclosures contained in the Integrated Report which includes coverage on our sustainability efforts and impacts. The Report comprises of an overview and about our profile that outlines our business model and the value generation process along with the Management Discussion and Analysis that consists of the business analysis, strategy and the six capital progress reports and disclosures pertaining to stewardship. All these reports should be read in conjunction with the Audited Financial Statements and other reports given in the Financial Reports section of the Annual Report. The Board through its delegated authority to the Finance Director/Chief Financial Officer governed the preparation and presentation aspects of the Integrated Annual Report that include Sustainability Reporting. I affirm that the Integrated Annual Report presented herewith has been prepared in accordance with the International Integrated Reporting framework of 2013, issued by the International Integrated Reporting Council (IIRC), and the GRI's G4 "in accordance - comprehensive" reporting framework.

Finance Director/Chief Financial officer
12th September 2017


MERCANTILE INVESTMENTS AND FINANCE PLC
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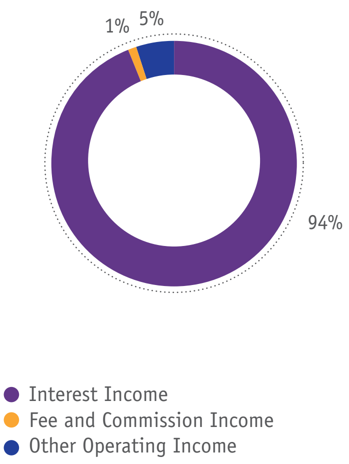
Capital Highlights

Financial Capital Highlights

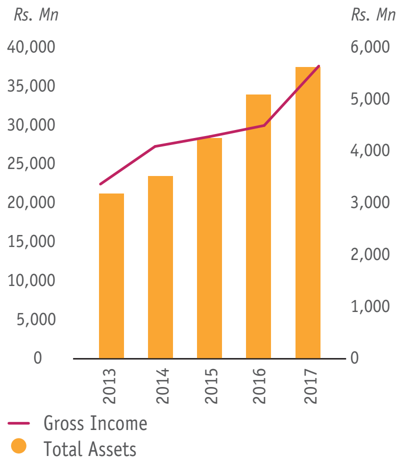
For the year ended 31st March	Achievement Actuals 2017 Rs.'000	Actuals 2016 Rs.'000	Change %	Financial Goals Budgeted 2017 Rs. Million	Forecasted 2018 Rs. Million
Results for the year					
Gross Income	5,645,533	4,500,275	25	> 5,200	> 6,700
Interest Income	5,286,060	4,301,828	23	> 5,000	> 6,500
Interest Expenses	3,136,218	2,098,378	49	< 2,400	< 3,500
Profit before Tax	313,679	802,645	-61	> 800	> 850
Provision for Taxation	111,665	297,626	-62	< 350	< 350
Profit after Tax	202,014	505,019	-60	> 500	>550
Financial Position at the year end					
Shareholders' Funds (Stated Capital and Reserves)	7,867,265	7,654,232	3	> 8,400	> 8,800
Deposits from Customers	17,017,674	15,815,590	8	> 18,000	> 19,500
Loans & Advances, Leases and Hire Purchases	28,645,276	25,053,528	14	> 30,000	> 32,000
Total Assets	37,492,664	33,964,707	10	> 38,000	> 42,000
Investors					
Gross Dividend	-	21,042	-100	> 45	> 45
Earnings per Share (Rs.)	67.20	168.00	-60	> 180	> 200
Dividends per Share (Rs.)	-	7.00	-100	> 15	> 15
Net Assets per Share (Rs.)	2,617	2,546	3	> 2,800	> 2,900
Ratios					
Return on Shareholders' Funds (%)	2.57	6.60	-61	> 8	> 8
Return on Average Assets (%)	0.57	1.62	-65	> 2	> 2
Interest Cover (Times)	1.10	1.38	-20	> 1.5	> 1.5
Dividend Cover (Times)	-	24.00	-100	>10	>10
Equity: Assets (%)	20.98	22.54	-7	> 25	> 25
Debt: Equity (Times)	1.43	1.17	23	<1.2	< 1.2
Dividend Payout Ratio (%)	-	4.17	-100	> 4	> 4
P/E Ratio (Times)	38.39	13.10	193	> 10	> 10
Non-Performing Loans Ratio (%)	6.92	3.39	104	< 4	< 4
Total Asset Growth (%)	10.39	19.56	-9	>15	>15
Advance Growth (%)	14.34	28.69	-14	> 20	> 12
Deposit Growth (%)	7.60	15.27	-8	> 15	> 15
Operating Profit Margin (%)	3.7	15.8	-77	> 15	> 15
Value Added per Employee (Rs. 000')	6,564	6,222	5	> 7,000	> 7,000
Interest Spread (%)	6.41%	8.01%	-20	> 8	> 8
Net Interest Margin (%)	7.42%	8.94%	-17	> 8	> 8
Statutory Ratios					
Liquid Assets (%)	10.81	11.73	-8	> 12	> 12
Core Capital Ratio (%) - Minimum Required 5%	17.17	19.35	-6	> 18	> 18
Total Risk Weighted Capital Ratio (%) - Minimum Required 10%	14.26	15.75	-3	> 15	> 15

In the backdrop of a challenging business environment, we made steady progress during the year in creating financial capital. As primary goals, we achieved sustainable increases in revenue, growth in the loan portfolio and generated steady pre-tax and post-tax profits.

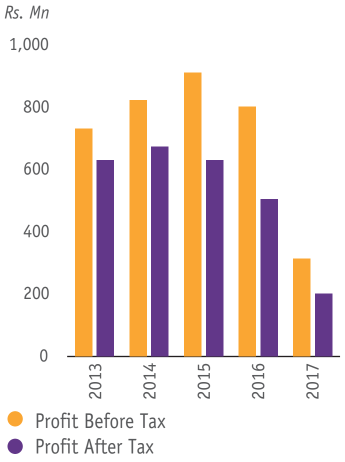
Comparison of Gross Income 2017



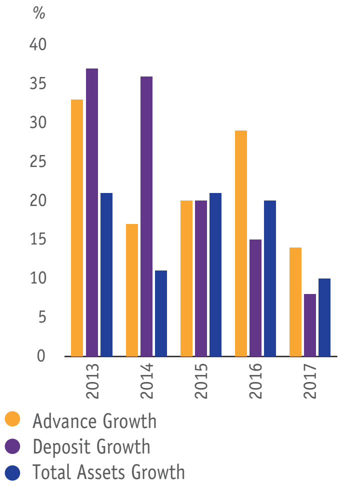
Total Assets & Gross Income



Profitability



Balance Sheet Growth



Gross Income grew by

25%

to Rs 5.6 Bn

Interest Income grew by

23%

to Rs 5.3 Bn

Total Assets grew by

10%

to Rs 37.5 Bn

Gross Advances grew by

14%

to Rs 28.6 Bn

Capital Highlights

Other Capital Highlights

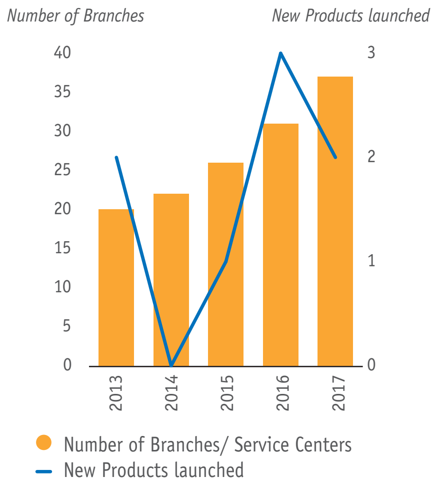
GRI G4 Indicator	For the year ended 31st March	2017	2016	Variance
Relationship Capital				
SO1	Total clientele	**48,884**	37,285	31%
SO1	New customers (Number)	**27,131**	20,330	33%
G4-DMA (Product Portfolio)	New products launched(Number)	**2**	3	-33%
EC1	Number of new business locations launched	**5**	5	0%
EC9	Percentage of purchases from suppliers: Head office, Colombo (%)	**60**	66	-6%
	Other locations of Sri Lanka (%)	**40**	34	6%
PR9	Significant fines for product/service (Rs.000)	**-**	-	0%
Human Capital				
LA1	Total workforce (Number)	**876**	738	19%
LA1	Recruitments in the year (Number)	**302**	264	14%
EC6	Local hiring of employees (%)	**70**	69	1%
LA1	Attrition rate (%)	**19**	15	25%
LA3	Retention rate after parental leave (%)	**40**	100	-60%
LA6	Number of injuries	**2**	4	-50%
LA6	Number of lost days	**26**	140	-81%
LA6	Absenteeism in days	**215**	296	-28%
LA 9	Training hours per participant as an average (Hours)	**9**	9.58	-7%
LA 11	Employee performance appraisal as a percentage of total workforce (%)	**77**	78	-2%
LA16	Employee grievances reported and resolved (Number)	**6**	5	20%
EC 3	Employee benefit liability - (Rs.000)	**171,772**	146,235	17%
HR3,5,6 & 12	Human rights violation	**-**	-	0%
Intellectual Capital				
	Brand Expenditure (Rs. Mn)	**60**	85	-29%
	Actual/Planned Investment in ICT (Rs. Mn)	**274**	-	0%
	ICT related user training (In hours)	**5,145**	2,381	116%
Social Capital				
SO1	Number of individuals responding on impact studies	**167**	90	86%
SO1	Number of CSR Beneficiaries	**4,218**	719	487%
SO3	Proportion of businesses reviewed for risk of corruption (%)	**100**	100	0%
SO4	Training on Anti money laundering (number)	**125**	211	-41%
SO8	Significant fines for violation of laws/regulations (Rs. Mn)*	**-**	-	0%
EC1	Community Investment cost (Rs.000)	**2,046**	7,053	-71%
EC1	Staff volunteered time on CSR (hours)	**4,152**	659	530%
Natural Capital				
EN 3	Electricity consumption in Head office(kWh)	**619,824**	667,308	-7%
EN 3	Total fuel usage (Litres)	**816,231**	605,770	35%
EN 8	Water consumption at Head office (Units)	**8,308**	8,304	0%
EN23	Paper recycling (Kg)	**2,756**	2,703	2%
EN 29	Significant environmental fines (Rs.000)	**0**	0	0%
EN31	Environment protection expenditure (Rs.000)	**357**	550	-35%
EN15-EN17	Total Carbon footprint (Tonnes)**	**2,447**	578	323%
G4-FS8	Green Lending (Rs. Mn)	**1,517**	859	77%

* Significant fines are defined as fines over Rs. 1 million.

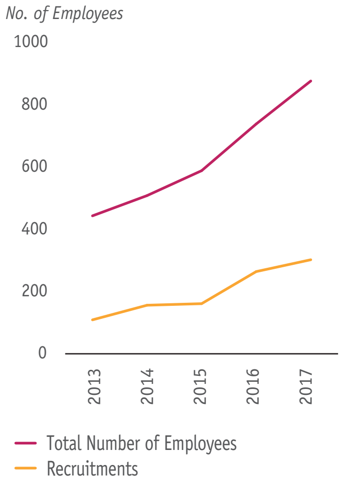
** Extended the carbon footprint review scope from head office to all locations from FY 2016/17.

The primary strategies we put forth brought us satisfactory results for FY 2016/17, impacting the various forms of capitals deployed, transforming them to meet various stakeholder expectations.

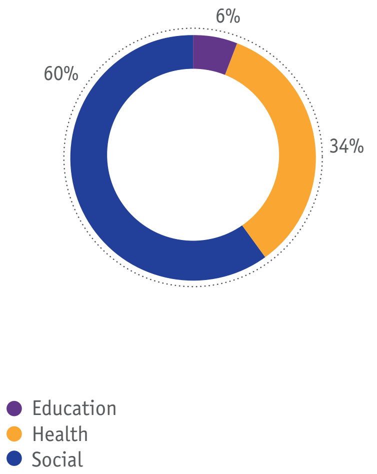
Customer Value Creation



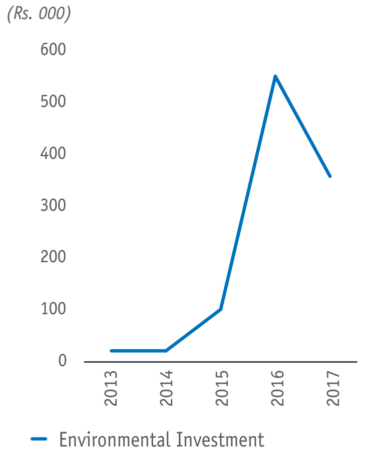
Growth in Staff Strength & New Recruitments



Number of Beneficiaries of CSR Initiatives -FY 2016/17



Environmental Investment



Total Customer Base grew by

31%

to 48,884

Number of CSR Beneficiaries grew by

487%

to 4,218

Total Branch network expanded by

16%

to 36

Total Staff Strength grew by

19%

to 876

Our Achievements and Milestones for 2016/17

Winning local accolades

Winning the CMA Excellence in Integrated Reporting Awards – 2016 –All Island Bronze Award

July 2016

Branch Opening

Opening of Veyangoda Branch

January 2017

All Island Bronze Award for Best Integrated Report and Award for being within the top Ten Best Integrated Reports at CMA Awards

July 2016

Winning the CA Sri Lanka - Finance Companies sector– Silver Award

December 2016

International Recognition

Winning three ARC Awards in New York for the 2015/16 Annual Report

August 2016

Branch Opening

Opening of Thambuththegama Branch

January 2017

A new core ICT solution

Managing Director with the international service provider

March 2017

Building natural capital

Tree Planting Project team joining to protect the environment with Rotarians

March 2017

Launching of the enhanced MI website

Managing Director initiating the website

January 2017

SAFA Annual Report Awards

First runner up in Integrated Reporting - Best Presented Annual Report Awards Competition held by South Asian Federation of Accountants

January 2017

Branch Opening

Extended our business presence to Central Province by opening a branch in Gampola

February 2017

Branch Opening

Extended customer reaching points in Western Province by launching Wattala Branch

February 2017

Branch Opening

Setting up of Avissawella Branch

March 2017

Chairman's Message

> "It was a challenging but fruitful period for us, as the Company was successful in implementing many of the strategies amidst the continued rise in interest rates and other demanding market factors to consolidate our position."

My Dear Stakeholders,

I welcome all of you to Mercantile Investments and Finance PLC's (MI) fifty-fourth Annual General Meeting and pleased to present the Company's Integrated Annual Report for the financial year ended 31st March 2017. It was a challenging but fruitful period for us, as the Company was successful in implementing many of the strategies amidst the continued rise in interest rates and other demanding market factors to consolidate our position. Our committed MI team starting from the Board stood determined and focused in fulfilling their individual targets, and this paved the way for the Company to achieve the annual targets, and towards its wider medium to long term goals.

> "In keeping to our visionary aspirations and integrated thinking, we continued to maintain clear interlinks between various components of our value creating process, to bring about that synergetic effect, which paved the way for us to generate value to our broad array of stakeholders."

A Value Creating Performance

The combined efforts of all the strategic business units and support divisions paved the way for the Company to meet key financial targets despite a lowered profitability. Through a wider business effort we were able to record a steady pre-tax profit of Rs. 314 Million and a Post- tax profit of Rs. 202 Million for the financial year ending 31st March 2017. However both pre and post-tax profits reported a notable decline of 61% and 60% respectively ,when compared with the previous year mainly on account of recording impairment charges. Further, as witnessed across the finance industry, the continued upward movement in interest rates and its resulting repricing effect impacted the cost of funding and core business margins which pegged back profitability levels against what was envisaged.

Triple Bottom Line Value Created

Broad Strategic Goals	Triple Bottom Line Value	Performance
Financial Capital » Enhance investor returns **Relationship Capital** » Wider customer base » Develop lasting bonds	Profit	» Total profitability before tax Rs.314 Million (Rs. 803 Million in 2015/16) » Revenue Growth 25% (5% growth in 2015/16) » Total lending book growth 14% (29% in 2015/16) » Deposit base growth 8% (15% in 2015/16)
Human Capital » Enhance employee capacity » Strengthen workforce **Intellectual Capital** » Build brand value » Strengthen ICT support **Social Capital** » Cater to wider wants of society	People	» New jobs created 302 (264 jobs in 2015/16) » Investment in automation (Actual & Planned) Rs. 274 Million (Rs. 9.4 Million in 2015/16) » CSR Projects completed 13 (13 in 2015/16)
Natural Capital » Safeguard nature » Control use of scarce resources	Planet	» Environment related investment Rs. 356,750 (Rs. 549,900 in 2015/16) » Green lending Rs. 1,517 Million (Rs. 859 Million in 2015/16)

Let me outline some of the salient aspects of our financial performance by drawing reference to some of the key performance indicators to reflect the efforts of the team, that resulted in success, and also discuss some of the areas in which we lagged behind the targets we set for ourselves, due to the challenging market dynamics that prevailed in the external environment.

Goals, Strategy and Capital Formation

In keeping to our visionary aspirations and integrated thinking, we continued to maintain clear interlinks between various components of our value creating process, to bring about that synergetic effect, which paved the way for us to generate value to our broad array of stakeholders.

The Board delegating through the Executive Directors and Corporate Management made significant strides in further development of MI's core business lines of lending and deposit mobilisation. Emphasis was given to critical success factors, which helped boost service standards and narrowed processing lead times. By pursuing our key strategic priorities, we boosted gross revenue primarily by emphasising on higher lending volumes and yields whilst maintaining our margins. We closely monitored the performance of our front line business teams, and made proactive decisions to eliminate or narrow the gaps identified. We intensified our marketing activities across the island and further strengthened the workforce which resulted in 302 additional recruits joining the Company. The satisfactory

Chairman’s Message

progress recorded during the twelve months concluding 31st March 2017, transformed most of our capital inputs both financial and intangible to create envisaged value.

Revenue Generation

Our expanding branch footprint was leveraged upon to maximise revenue generation, to identify new business and to cement strong bonds with existing clientele. We experienced steady growth in our lending volumes which resulted in the loan book growing buoyantly by 14% year-on-year. In contrast, the deposit base grew moderately increasing by 8% year-on-year. In the backdrop of rising market interest rates, we were conservative in the mobilisation of deposits that were deemed relatively more costly than other sources of funding available, and hence, we were able to access less costly sources of funding through borrowings on the strength of our brand which is synonymous with financial stability and integrity.

Despite close management of pricing and funding, it was challenging to maintain the required net interest margins which dropped by 17%, year-on-year to 7.42%, behind targeted levels. Our core business of lending remained the main source of revenue for the Company, contributing 90% to gross revenue while the non-fund based income being the other main source of revenue came primarily from fee and commission, trading in shares and the receipt of dividends.

MI’s microfinance business which is still in a nascent stage together with other term based lending drove overall yields while traditional lease financing continued to generate steady business growth albeit at relatively lower yields. We introduced new products such as auto-drafts and also promoted personal and corporate forms of lending that included property backed funding done on a moderate scale.

Assets Growth and Quality

We experienced a 10% growth in total assets which advanced to Rs. 37.5 Billion as at the reporting date, mainly driven by the growth in the loan book, while equity investments remained the other large component of total assets.

As a consequence of product growth and diversification, we were cautious about the increasing credit risk and took steps to strengthen our recovery process to mitigate the impact to asset quality. Despite these efforts, the non-performing ratio moved upward to 6.92% due to a few large accounts falling into arrears but backed adequately by security. The impairment charges in total for the year stood high at Rs. 625 Million up by 166% impacting overall profitability.

Sustainable Impact

As an organisation that envisions creating sustainable impacts that are need based and reflective of longer term view and benefitting all our key stakeholders, we aligned our business model to cater to a wide array of stakeholder needs. We went beyond commercial boundaries to create value for society and the environment, adopting a streamlined effective approach. Triple bottom line value creation is at the core of our corporate planning process and remained embedded in our unique business model. Through this unique model we continued to enhance key stakeholder value, transforming the six main forms of capital, to widen our triple bottom line impact, bettering our performance on numerous facets.

Sustaining Profits

The financial performance achieved for the period under review in challenging conditions highlights are commitment towards our primary objective of delivering sustainable returns for our investors and value to our key stakeholders.

> "As an organisation that envisions creating sustainable impacts that are need based and reflective of longer term view and benefiting all our key stakeholders, we aligned our business model to cater to a wide array of stakeholder needs. We went beyond commercial boundaries to create value for society and the environment, adopting a streamlined effective approach."

The expansion strategy we undertook during the last decade has been fruitful towards achieving our sustainability goals. We have extended credit facilities to our clientele based on the sustainability precepts of inclusivity and diversity. Such credit facilities and deposit mobilisation has been made easier to access through our efforts to increase our footprint across the country, improving our reach to all through our network of 36 branches/service centres, with the opening of five more branches this year. Through the growth of our business we have been able to penetrate deeper into the outskirts of Sri Lanka, going beyond the Western Province, to build business relationships that have been mutually beneficial and rewarding.

Our aim is to afford our customer base a value proposition that provides access to ethical funding through our range of financial solutions including microfinance which has been customised based on customer needs and lifestyle changes, and driven by an increase in per capita incomes with the country moving to middle income status.

Our approach will continue to support life style changes across all economic strata, age groups, ethnicities and gender, encouraging entrepreneurship and wealth creation for individuals, the SME sector and local corporates. It also encompasses conserving and protecting the environment for future generations. All of the above have resulted in value release to all our stakeholders and contributed to the development of the Licensed Finance Company sector and long term growth and prosperity of our nation.

Sustaining the Value of People

From the perspective of human capital, we were committed in our efforts to widen employee knowledge through needs based training and human development activities, and continued to motivate top performers through a robust performance management system that is linked to rewards and recognition. The corporate leadership team has also provided the required morale support, guidance and mentoring. As witnessed in the past, the growth of our business has resulted in new job opportunities and roles. We managed to increase the total workforce by 19% year-on-year, through our recruitment strategy during the year under review.

We capitalised on our expanding presence, to afford people easy access to credit, to better their lives and livelihoods. Our budding microfinance business more importantly has paved the way for MI to have close links with communities, to build lasting meaningful bonds. As the Chairman, it is my wish that MI continues to identify ways of enriching communities, particularly providing funding to those who have had little or no access to credit, to build their lives, at a juncture when the nation as a whole is slowly but steadily recovering from past challenges.

I would also like to commend the Sustainability Governance Committee for their commitment towards executing the corporate social responsibility initiatives, in supporting the poor and the less privileged beyond commercial boundaries, and for the community service extended which has been worthy and effective.

Sustenance of the Planet

Having experienced rapid expansion in organisational presence within the last five years, I am pleased with our efforts this year in identifying ways of reducing our operational impact on the environment. For the first time, we obtained the Greenhouse Gas emission levels emitted for the total Company, whereas last year estimations were limited to the Head Office. I am satisfied with the internal green procedures we adopted to cut down on use of natural resources and the initiatives kick-started this year in naturalising our emissions through the tree planting campaigns and additional waste control measures embraced during this period to eliminate pollution.

Our Corporate Governance Prerogatives

As the Chairman, I affirm the Board’s commitment in institutionalising an effective governance and risk management framework across the organisation. While adhering to regulations on corporate governance directives, we also voluntarily adopted the best governance practices recommended by the SEC and CA Sri Lanka, which has aided us significantly in the way we govern the affairs of the Company.

We carried out independent reviews of our internal processors, ensuring that embedded controls remain robust and effective particularly strengthening internal controls relating to our deposit operation. I am also happy to highlight the steps taken to increase the bench strength of the internal audit department during the year, and the risk based audit approach adopted as means of auditing operational areas and locations that are deemed riskier.

Under the supervision of the compliance officer, we strengthened internal Anti-Money Laundering (AML) procedures and issued a revised AML policy document in line with the Gazette 2016. As the Chairman, I confirm that no known material violations of disciplined business conduct and ethical requirements of the Company have taken place during the year, at the Board level as well as at other levels of the corporate hierarchy.

> "We capitalised on our expanding presence, to afford people easy access to credit, to better their lives and livelihoods. Our budding microfinance business more importantly has paved the way for MI to have close links with communities, to build lasting meaningful bonds. As the Chairman, it is my wish that MI continues to identify ways of enriching communities, particularly providing funding to those who have had little or no access to credit, to build their lives, at a juncture when the nation as a whole is slowly but steadily recovering from past challenges."

Future Prospects and Challenges

The progressive economic activity taking place and improving international sentiment towards Sri Lanka is bound to provide ample

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opportunities for the business community and entrepreneurship in the foreseeable future. We expect the living standards of people and per capita income levels to improve as the private sector takes a greater stake in partnering the Government in developing the infrastructure of the country. In partnering the Government, the private sector will focus on supporting the poor and middle class, play an active role in empowering people, identify ways to uplift the standards of education, health, sanitation and housing, while creating employment opportunities.

Tourism which is forecast to continue its growth momentum and with its cascading effect of transferring wealth across all income groups will also spawn young entrepreneurs and opportunities for wealth creation.

> "While reiterating the noteworthy performance displayed by all core divisions and support functions, the dedicated efforts of our workforce yet again made it possible to accomplish most of our operational goals, to conclude the year satisfactorily. I commend all those who were recognized as top performers during the year and send my appreciation to the whole MI team for their individual contributions made towards the organizational goals and aspirations."

The reversal in the reform momentum, increases in public debt from further devaluation of the rupee, the decline in reserves, loss making state enterprises and widening trade deficit are a few of the major constraints which weigh against the country’s sound growth potential of 4.4% of GDP forecasted by Standard and Poor’s for the period 2017-2020.

Despite the economic upturn and wider opportunity for business growth, the finance companies will remain somewhat sluggish due to the slump in vehicle registrations amid higher duty structures, stricter financing conditions imposed on the vehicle sales market, and controls placed on credit growth. In this context, we can expect the industry to stay innovative in widening its scope and audience. I believe the sector will reinvent itself to capitalise on emerging opportunities, moving away from its standard lending options to more sophisticated forms. In this transformation process, technology will play a significant role for the Industry.

In the midst of this economic transformation, MI is well set, having made an all-out plan to exploit emerging opportunities, based on future trends and forecasts. We understand the rapidly changing nature of the finance market and people’s preferences. We expect societal habits and expectations to change as economic development takes place across regions. Our task at this juncture would take on a wider role like others in the business community. We hope to be part of the nation’s rebuilding process, a vessel that facilitates trade opportunities and one that creates job opportunities and benefits to the wider community. I believe, we as veterans in the financial services sector, should pitch in to support future entrepreneurs, whatever their status in life maybe.

To fulfil MI’s wider set of goals and visionary aspiration, our workforce will be constantly nurtured, up-skilled and motivated. I am sure MI’s positive impact to the economy, society and the environment will increase overtime, as we intensify our activity, enter into new territories, embrace new technology advancements and business partnerships than we did before. MI possesses the required capital, be it the financial capital or intangibles such as business intelligence, people skills, and an unblemished track record to reach out to potential business segments and emerging community needs.

Appreciating Tireless Efforts

Indeed, this year's performance cannot be attributed to few individuals, but was certainly an all-out effort from the whole MI team, from all fronts of the organisation, to stretch and go that extra mile in achieving success. As the Chairman, I take this opportunity to thank all my fellow members of the Board for their invaluable contribution, and for providing continued guidance and advice to the management, for effective governance of the organisation.

While reiterating the noteworthy performance displayed by all core divisions and support functions, the dedicated efforts of our workforce yet again made it possible to accomplish most of our operational goals, to conclude the year satisfactorily. I commend all those who were recognised as top performers during the year and send my appreciation to the whole MI team for their individual contributions made towards the organisational goals and aspirations.

I would like to take this opportunity to thank the Governor, Deputy Governor, Director Non-Banking Supervision Department and to all relevant staff of the

Central Bank of Sri Lanka for their continued guidance and for the cooperation extended to us when needed.

I take this opportunity to also thank all our customers and other financial business partners, for continuing to display your loyalty and keeping the faith in the Company at all times. Your continued loyalty has inspired us to look for better ways in serving you and encouraged us to raise the bar in whatever we do. A special note of thanks is also extended to all our intermediaries, namely the agents and other transacting parties who remain an integral component to MI's business growth.

Finally, my gratitude extends to our investors, for standing always beside the Company in both good and challenging times. While thanking you again for placing immense trust in the Board, we affirm our commitment towards enhancing shareholder wealth and striving for sustainable triple bottom line value, for the benefit of all our key stakeholders. MI will continue its journey with much optimism, having set an ideal platform for the future, to operate as a highly sustainable business, while remaining a socially responsible corporate citizen to build a more sustainable society and a nation.

Saro Weerasuriya
Chairman

12th September 2017

Managing Director's Review

"It was pleasing for me to observe the gradual increase in the influx of new customers which we attracted from most customer segments on the strength of our Brand, which is known for its financial strength, stability and personalised service quality, which has been experienced over the 50 plus years of service to the Sri Lankan community."

"Post war economic development and the rejuvenation of almost all key sectors that include the tourism industry, propelled the finance industry growth, stimulating especially motor vehicle financing, corporate funding and funding linked to property development."

Core Business Consolidation

Going into our fifty-third year of operations, our emphasis was focused on consolidating our business operation across the country; capitalising on the increased footprint and leveraging on the brand identity of strength and stability that we have earned over the fifty plus years in operation. Efforts aimed at developing our core business of lending and deposit mobilisation, remained very fruitful and went according to plan. The Board together with the management team remained committed to achieving our business strategy and was able to successfully implement our strategic actions to outperform rather challenging targets set, in somewhat volatile business environment. There was significant investment made in retaining existing high performers and acquiring new talent to support marketing and operational activities. We also took necessary steps to embrace more advanced technology, to support ICT, with a view to enhancing our operating platform and operational efficiency and productivity.

We opened branches in five new locations during the year under review, increasing our presence further. We were successful in attracting new customers and also ensured that we continued to cement the strong bonds with our existing clientele. It was pleasing for me to observe the gradual increase in the influx of new customers which we attracted from most customer segments on the strength of our Brand, which is known for its financial strength, stability and personalized service quality, which has been experienced over the 50 plus years of service to the Sri Lankan community. In expanding our lending portfolio, we continued to promote our budding microfinance lending business to low income earners. With the boost of additional micro finance units coming into effect since the last twenty four months, we were successful in growing the microfinance portfolio at an astounding pace. The continuous growth of Mercantile Investments (MI) customer relationships has resulted in empowering the poor and middle class, towards fulfilling their wants and unmet needs, for greater prosperity and improvement in their lifestyles.

Opportunities and Challenges Faced

In spite of the economic growth slowing down globally with just over 3% increase in world output, future prospects look promising due to the visible improvements in international trade and reducing unemployment levels. Emerging economies continued to play a significant role in tandem with the dominant advanced economies showing greater resilience to economic challenges than before. From the Asian region, India continued to be a growing force, a close counterpart to a prospering China. As a nation having close ties with the Asian region, Sri Lanka’s improving global sentiments and the Government's forward looking policies on boosting international trade and the inflow of foreign direct investments, supported local industries to perform better this period.

The Sri Lankan economy progressed steadily with real GDP growing in 2016 by 4.4%, compared to 4.8% recorded in 2015. Post war economic development and the rejuvenation of almost all key sectors that include the tourism industry, propelled the finance industry growth, stimulating especially motor vehicle financing, corporate funding and funding linked to property development. However, the persistent rise in domestic interest rates, and the limitation of liquidity levels in the market coupled with targeted government measures controlled finance industry credit growth which averaged a moderate 21% year-on-year growth.

Despite the business opportunities for corporates, the Licensed Finance Company sector, encountered a somewhat challenging year. Over 300 basis points upward movement in interest rates impacted the industry’s funding costs, exerting further pressure on already squeezed margins. Restrictions placed in vehicle backed lending, also pegged back the industry’s leasing business and related lending. In spite of this, the industry demonstrated its resilience, sustaining growth through innovation and aggressive thinking, directing funding towards plethora of funding needs of individuals that ranged from grass-root levels to large disbursements to high-net-worth clients and also widening funding support to corporates.

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Performance in a Nutshell

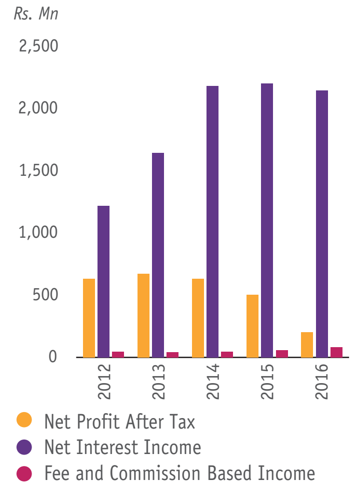
It was a somewhat modest year for MI in terms of profitability , as the company recorded a lowered Pre-tax profit of Rs. 314 million and a post- tax profit of Rs. 202 million, behind anticipated levels. This reflected a decline in pre- tax and post-tax profits of 61% and 60% respectively, pegged back mostly by the increased costs resulting from repricing of the deposit base and expenses incurred on recent operational expansions and moreover recording higher levels of impairment charges for the year.

Salient Achievements Capital Wise

Capital	Indicator	2015/16	2016/17	YOY Variance Increase/ (Decrease)
Financial	» Net Profit After Tax (Rs.Mn)	505	202	(60%)
	» Gross Revenue Growth (%)	5	25	400%
	» Total Lender Portfolio Growth (%)	29	14	(52%)
	» Total Depositor Portfolio Growth (%)	15	8	(47%)
	» Total Assets Growth (%)	20	10	(50%)
Relationship	» Number of Borrowers	36,996	50,352	36%
	» Number of Branches	31	36	16%
	» Number of Depositors	4,300	4,578	6%
Human	» New Jobs Created (Nos)	264	302	14%
	» Staff Turnover	114	164	44%
Intellectual	» Investment in Automation actual/planned (Rs. Mn)	9.4	274	2,815%
	» New Processors Automated (Nos)	12	11	(8%)
Social & Natural	» Total Community & Green Investment (Rs. '000)	7,053	2,195	(69%)
	» Number of Beneficiaries	719	4,218	487%

In somewhat challenging business conditions, we focused on boosting our net interest margin which stood at 7.42% lower than expected and behind the industry average of around 8%. In the light of this, strategic measures were taken to aggressively expand lending volumes as a means of sustaining anticipated interest income. As a result, we recorded a total gross revenue of Rs. 5.6 Billion, reflecting a year-on-year increase of 25%. The main contributor to gross revenue being the interest income was up by 23% with a 94% contribution to gross revenue. Nevertheless, Net Interest Income (NII) remained marginally lower than last year at Rs. 2.1 Billion, pegged back by the relatively faster rise in interest costs on repricing compared to lending yields, exerting pressure on core margins.

Profitability & Revenue



From a balance sheet perspective, total assets advanced by 10%, reaching Rs. 37.5 Billion, boosted by the expanding lending book while total shareholders funds remained at a 3% marginal growth level. Shareholders equity growth was lower on account of the pegged back profitability posted, impacted by the increased funding cost and a Rs. 625 Million of impairment charges.

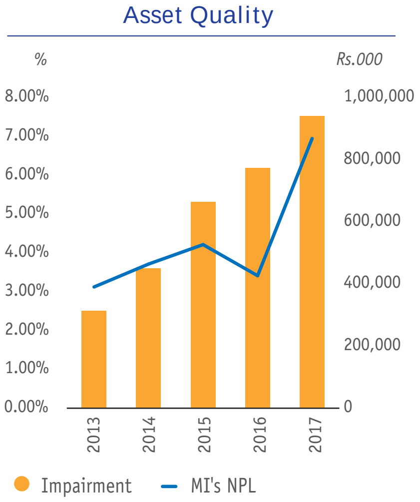
In pursuing our financial goals, we stuck to a clear game plan, focusing on improving key performance variables that generate revenue, maintain asset quality while optimising costs. These chiefly include;

Recording a noteworthy 14% growth in lending book supported by a 36% increase in number of borrowers

The total loans and advances portfolio surpassed the Rs. 28 Billion mark, boosted by a 12% growth in lease financing, with noteworthy growth recorded in specific categories of loans and advances. i.e. vehicle loans 32% and personal and corporate lending 84%. Moreover, microfinance lending growth stood phenomenal at 115%, propelling overall volume increase and also helping to boost lending yields, considering its higher return advantage. Nevertheless compared to last year, MI's credit growth slowed down by 52%, in keeping to similar trends of the finance industry. Therefore to maintain projected lending growth targets, we carried out frequent marketing campaigns, creating awareness of our product mix across key regions, attracting new clientele from various segments of society.

Asset Quality Maintenance

Despite an ethos of stringent measures of credit control and actions aimed at efficient recovery of arrears contracts, non-performing lending ratio stood at 6.92%, owing to few large facilities falling overdue on their repayments. However, adequate collateral was provided against these credit exposures and recovery efforts were expedited to collect total dues. It is noteworthy of mention that the coordinating efforts of the recovery division with the internal valuation and asset disposal unit together with the legal division, resulted in annual collection levels being commendably maintained at over 90% with stringent recovery action expedited where necessary.



Broad-based Deposit Mobilisation

The total deposit outstanding stood at Rs. 17 Billion and the total depositors in number promisingly increased by 6% YOY. However, deposit growth remained moderate at 8%, slowdown based on our funding strategy of optimising cost of funding between deposits and borrowings based funding. The exceptional efforts displayed by our branch staff responsible for deposit mobilisation, towards increasing the contribution made by branches to the overall deposit base and building a larger base of retail clientele is noteworthy and commendable.

Human Capital Development

In keeping with our ultimate aim of a sustainable business model, we invested in the nurturing of our people, structuring effective training and career development programmes that helped them acquire the necessary skill sets that would make them enablers in a growing competitive environment. By intensifying training activities, we afforded greater learning opportunities for staff, increasing annual total training hours per employee astoundingly by 129% year-on-year. Based on our performance appraisal system, we identified top performers bi-annually and concentrated on boosting productivity whilst sustaining the desired motivational levels. During the year, we made plans to move to a more sophisticated human resource information system which will result in improved management information that will lead to better business decisions and an empowered workforce.

Cost Optimisation

At a time when overhead expenditure continued to escalate on account of operational expansion, we understood the need for an ongoing review of costs and the need for cost consciousness with the aim of building a culture of cost optimisation. We appointed a cost controller and a supportive team to monitor and report areas of duplication, wastage and recommend measures to cut down recurring costs that were viewed as being excessive. With the recruitment of an experienced procurement officer, we also streamlined our procurement processors and also managed to negotiate better pricing and quantity discounts that led to further savings.

> "As we expand our operations and inculcate our sustainability ideologies in the way we do business, we hope to increase our positive impact on the economy, society and the environment. We hope to further align internal processors towards this objective and also expect to extract more measurable data so that we could better assess our impacts, for the benefit of our stakeholders."

Good Governance Initiatives

Our corporate governance framework and policies and procedures built up over the years assisted the Board and the management to manage the business with prudence having identified the relevant risks and opportunities. This structure and sound governance approach enabled the management to exercise a high level of oversight, in driving the business towards achieving its corporate goals and sustainability agenda. Robust and effective controls together with audit checks were implemented across the business to ensure compliance with regulatory and statutory requirements and safeguard corporate assets. With the finance industry navigating

Managing Director's Review

a somewhat challenging phase, our Board remained focused on the performance milestones of the Company while keeping abreast with the industry dynamics in directing the corporate affairs of the Company.

Under the effective counsel and leadership of the Board, we implemented best-in-class practices such as regular submission of Board Sub-Committee activity reports to the Board that included a detailed compliance report being submitted monthly during the year under review. Moreover, the Board was able to obtain assistance of an external ICT consultant, to carry out an AS IS study and outline MI's future ICT strategy based on a needs analysis that was carried out to arrive at a comprehensive ICT solution, that involved a total migration to a renowned core operating system over the duration of the next financial year.

The Board was instrumental in formulating the risk agenda for the Company and the management of risk and mitigating actions ranked high on the list of priorities identified by the management team. Additional supportive mechanisms were introduced to comply with the 2016 Gazette requirements on anti-money laundering and new procedural changes were formalised to ensure risk management processes were robust and effective.

Operating under Sustainable Ethos

Our commitment towards development of a sustainable business model that not only strives for continued investor returns but also addresses the broader impacts on the economy, society and promotes a liveable environment is deemed high priority in the way we do business. These ideologies remained well embedded in our strategic thinking, operational plans and actions. A number of initiatives executed went that extra mile in greatly supporting members of society to better their lives and livelihoods. I am proud to observe MI's value creation has been beneficial to society and we have been able to further embed value with greater depth and breadth than in years past.

> "In somewhat challenging business conditions, we focused on boosting our net interest margin which stood at 7.42% lower than expected and behind the industry average of around 8%. In the light of this, strategic measures were taken to aggressively expand lending volumes as a means of sustaining anticipated interest income. As a result, we recorded a total gross revenue of Rs. 5.6 Billion, reflecting a year-on-year increase of 25%. The main contributor to gross revenue being the interest income was up by 23% with a 94% contribution to gross revenue."

We were able to empower individuals of society through our approach of socially responsible inclusive funding support that improved livelihoods and income generation. Numerous family units and communities were benefited by this approach in meeting their unmet or poorly met needs and making the requisite lifestyle changes afforded by an economy that is moving towards middle income status. The social impact MI has created thus far has been overwhelming, particularly in the microfinance services extended from over 1,300 centres across the island, which no doubt will continue to bring economic freedom and prosperity to many.

I would like to also commend the philanthropic efforts of the Sustainability Governance Committee, in identifying societal needs beyond just funding, by supporting especially the poor and less privileged through worthy CSR projects. In our own way, we strived towards addressing their lack of basic needs through the supply of adequate shelter, disaster relief and other community assistance, to people living in difficult conditions and those effected by the droughts.

The tree planting campaign initiated for the second time, conducted during this year in coordination with the Rotarians was another significant step taken in fulfilling our pledges towards the safeguarding of our planet and its habitats. To showcase MI's efforts this year in creating a more sustainable enterprise and a resolute society, our Integrated Annual Report for the second consecutive year was prepared in keeping to the Global Reporting Initiative's (GRI's) G4 "In accordance-comprehensive" reporting framework.

Future Outlook

Economy and LFC sector

The business community is optimistic as economic development activity motors along, with most sectors led by tourism reaching new heights. The current stable political climate and macroeconomic policy coupled with improving international sentiment should propel both the national output and per capita income levels to move on a steady upward trajectory. Apart from the ongoing construction and infrastructural development activity taking place, investments in large scale commercial projects that include the port city project, are bound to stimulate economic growth in the medium term. We can also expect the flow of foreign direct investment to improve in the foreseeable future, fuelling the local market and the stock exchange. In spite of the growing optimism, there will be challenges to contend with. The high interest rate regime will remain a constraint in fast tracking credit growth and economic activity in the short term but should reverse over time. Another concern would be the continued pressure exerted on the exchange rate and the impact it will have on import costs.

Looking ahead, Finance Companies will need to stay innovative and bold in their actions so as to improve yields and to have tight control over funding cost. It is apparent that the vehicle sales market will be saddled with the prevailing high import duty structure and the recently introduced controls on granting of vehicle backed credit which will further dampen portfolio growth for the Industry. In this backdrop we can expect greater product diversification in the area of loans and advances and collaborative partnerships to take place within the sector. The financial services sector will have to adopt more resilient practices to stay competitive and also counter risks through greater investment in compliance and governance frameworks.

How We Plan to Face the Future

MI's business focus for the next few years will primarily revolve around consolidating its position outside the Western Province, by focusing on building regional presence in new markets that MI has entered. We are confident of our corporate strategy and business model in generating the required revenue, to stay a competitive force in the industry. The Board, corporate management and staff will stay committed and well attuned to changing trends and preferences of customers, products, markets and other changes happening at a macro level. I stay committed and affirm my commitment toward MI's continued sustainable value creation.

To generate the required sustainable performance levels we hope to monitor our KPI's and KRI's closely and keep a close tab of following key focus areas;

Expand Revenue Market Share to 4% by 2020

As financial markets become more concentrated and competitive, we hope to introduce more innovative solutions to the market, that will help us increase our market share to 4%. We are determined to capitalise on emerging opportunities that include funding for large projects, non-collaterialised based credit and specific corporate funding requirements to capture new business. Further, in pursuit of new revenue streams, we hope to tap on the middle and lower income earners who are willing to become champions of economic change, whilst national development activities continues to take place from all around.

> "In keeping with our ultimate aim of a sustainable business model, we invested in the nurturing of our people, structuring effective training and career development programs that helped them acquire the necessary skill sets that would make them enablers in a growing competitive environment. By intensifying training activities, we afforded greater learning opportunities for staff, increasing annual total training hours per employee astoundingly by 129% year-on-year. Based on our performance appraisal system, we identified top performers bi-annually and concentrated on boosting productivity whilst sustaining the desired motivational levels."

Operational Decentralisation with Close Oversight

Having customer convenience in mind, we expect to complete the decentralisation of core business activities by the next financial year. Comprehensive automation of our key processors is expected to speed up and improve the ease of doing business at branch level by eliminating bottlenecks. In like manner, we hope to strengthen the risk, compliance and audit functions by widening their scope and investing in more resources that will provide greater insight into risk identification and risk mitigation.

Increased Investment in People

Cultivation of people's knowledge and capability in line with market changes will remain another high priority. Training and development will aid in fulfilling future human resource demands. We hope to maintain a highly motivated skilled workforce geared for future challenges, whilst harnessing team play and harmony among employees.

Embracing Advanced Technological ICT Support

By focusing on technology, we hope to drive efficiency and productivity by automating key business processes. We also plan on investing in data mining techniques that will provide us with quality and timely management information that will result in better quality business decisions. I am happy with the progress made in enhancing our system capabilities during the last financial year and hope to stay firm on our decision to migrate to a more sophisticated system by the end of the next financial year.

Managing Director's Review

Upholding Sustainability Ideologies

As we expand our operations and inculcate our sustainability ideologies in the way we do business, we hope to increase our positive impact on the economy, society and the environment. We hope to further align internal processors towards this objective and also expect to extract more measurable data so that we could better assess our impacts, for the benefit of our stakeholders. As an integrated thinker, we hope to better interlink activities to derive the anticipated sustainable synergetic effect, for matters deemed material to the Company.

Tributes and Acknowledgements

It is with a deep sense of pride and gratitude that I take this opportunity to thank the whole MI team for their dedicated efforts, of being able to achieve key targeted performance standards in challenging conditions. I also take this opportunity to thank our Chairman and the Board of Directors, for the expert advice given and continued guidance extended to me. Indeed your contribution remains an invaluable source of strength to all of us.

I thank the new Governor of the Central Bank and his able staff for their support and for the cooperation extended to us.

A special word of thanks is also extended to our valued customers, for choosing MI to be your trusted business partner. We are inspired and encouraged by your continued loyalty towards the Company.

I would like to thank all our shareholders for the trust they have placed in our capability as a team and conclude with words of optimism to all. Having enjoyed the fruits of a highly successful enterprise for over fifty years, we move ahead to the next fifty years and beyond with immense vigour and much optimism, knowing that we are well placed to take advantage of the ongoing economic transformation. As appropriately highlighted in our theme, as a **"Prudently"** governed organisation, we hope to display exemplary governance when reaching our goals, ensuring that the interest of our key stakeholders is protected from future risks and challenges.

Gerard G. Ondaatjie
Managing Director

12th September 2017

About Us

sta•ble

adjective

1. not likely to give way or overturn

---

2. firmly fixed

Synonyms

1. steady 2. reasonable, sensible

About Us

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Our Vision, Mission and Value system 32 - 33
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About Us

☑G4-7

Nature of Ownership and Legal Form

Mercantile Investments and Finance PLC (MI) is a Licensed Finance Company under the Finance Business Act No. 42 of 2011, listed on the DiriSavi Board of the Colombo Stock Exchange. MI is also a public limited liability Company, incorporated in Sri Lanka on 15th June 1964 under the Companies Ordinance No. 51 of 1938 and re-registered under the Companies Act No. 07 of 2007.

☑G4-56

Our Vision, Mission and Value system

Our Vision

To be a leading financial institution committed to excellence in our sphere of activities with a deep sense of social responsibility.

Our Mission

To achieve our strategic vision, we would harness all our resources in the most productive way to be prudently managed and to serve our valuable customers in keeping with national objectives.

Key Values

» Customer bondage

» Recognising employee efforts

» Team spirit

» Securing investor capital

» Socially responsible and ethical actions

» Fair but aggressive competitor

Key Principles

» Fulfil customer needs beyond expectations

» Create lasting bonds with people

» Deliver customers a service that is world class

» Business practices to compliment core values

Our Sustainability Philosophy

As our business journeys towards attaining commercial excellence, we are committed to the precept that it should be enacted with a deep sense of empathy towards building a sustainable tomorrow for all.

Our Sustainability Mission

To fulfil corporate obligations towards our key stakeholders focusing on economic, social and environmental needs, which in turn will support in building a sustainable nation.

Our Sustainability Policy

The Company commits itself to upholding an effective sustainability governance framework and business processes designed and developed on the precepts of sustainability to ensure economic, social and environmental needs of stakeholders are fulfilled on an ongoing basis, without compromising the future. As the Company focusses on wealth creation the resultant benefits cascade down to our key stakeholders so that they will derive value from our organisational activity, to enrich lives, develop communities and conserve the environment, thus leading towards a more satisfied and sustainable nation.

The Company History and Style of Management

MI commenced business in 1964, under the visionary leadership of its founder Chairman George Ondaatjie. The exemplary and visionary leadership displayed by our founder has continued to influence the way we manage our business which now spans over five decades and has transformed the enterprise into a highly successful organisation in the Licensed Finance Company sector (LFC). During these successful years, MI has remained deep rooted to its visionary aspirations, not only excelling in its sphere of business but displaying true commitment towards its overarching philosophy of sustainable growth, profitability and resource development though which it has met with a wide array of stakeholder expectations and been able to deliver value over the last five decades. In keeping to MI’s fundamentals and value system, the Company under the leadership of the Managing Director, Gerard Ondaatjie, was able to successfully expand its business operation rapidly in the last decade. The Company now operates from over 30 locations in all key districts of the country, catering to the funding needs and providing services around deposit mobilisation to those seeking attractive returns and competitive lending rates from a secure enterprise.

MI Board is structured with the right blend of individuals, who come from varying professional backgrounds and possess the necessary skills to guide the organisation effectively towards achieving its sustainability agenda, in a prudent manner. The Board is amply supported by a highly skilled management team and a capable workforce that remains focused on executing the planned strategy and operational activity for the ultimate achievement of organisational objectives. The tone at the top, right from the Board of Directors, cascading down to other levels of the hierarchy, reflects one of vigour, but has always stayed conservative in matters deemed risky and volatile. The culture practiced empowers committed individuals to remain creative and to display a high degree of ethics and integrity at all times.

In a nutshell, the enterprise remains focused on sustaining value creation to all key stakeholders through the provision of ideal financial solutions to customers and wealth of other initiatives carried out to enhance stakeholder value. The enterprise continues to uphold the right strategy to enhance its six forms of capital, creating investor value and a lasting positive impact on the economy, society and the environment.

☑ G4-4

Primary Brands, Products and/or Services

Being in the business of the provision of credit facilities and the mobilisation of deposits, the Company has expanded its product portfolio to cater to a wider array of customers and market segments, promoting most of the products under its umbrella brand “MI”. During the last decade, MI has diversified its lending product range from providing traditional lease and hire purchase financing to term based lending such as personal and corporate loans, pledge loans, property mortgage loans with the latest addition being microfinance. Fixed deposits remain the Company’s main deposit mobilisation product while MI’s savings products have gained popularity and are being further developed to meet with the requirements of a changing economic and regulatory landscape and customer expectations.

About Us

Output products from MI’s business

Lease Financing

Lease facilities are granted mainly against vehicles and machines in accordance with the Finance Lease Act No. 56 of 2000. MI is proud of the trust and conviction that is placed upon them from loyal leasing customers.

- » Vehicle Leases
- » Machinery Leases
- » Operating Leases
  Operating Lease services at MI are carried out on special request for motor vehicle leases at a fixed monthly sum.

Hire Purchase Financing

In keeping to the Consumer Credit Act No. 29 of 1982; lending facilities are given mainly against vehicles and machines that have been registered. This instalment-based service provides MI customers to plan out their funds for maximum benefit, prior to final ownership.

- » Vehicle Hire Purchase
- » Machinery Hire Purchase

Vehicle Loans

Lending services are offered against registered or unregistered vehicles. Further, prompt application processing guarantees customers of MI a pleasant experience.

Term Loans

At MI, we provide a range of term based funding which are customised to serve the diverse needs of all Sri Lankans. These are lending services that are fixed term based, either secured or unsecured.

- » Corporate Term Loans
- » Personal Loans
- » Professional Loans
- » Working Capital Loans
- » Auto Draft Loans
- » Cheque Loans

Property Backed Lending

Lending services extended against property given as security under a mortgage bond. At MI, we understand the needs of our customers and offer time-sensitive solutions.

Microfinance Lending

Microfinance services are offered to low income earners, providing them the opportunity to become self-sufficient and self-employed enabling individuals to improve their quality of life.

Fixed Deposits

Fixed Deposits at Mercantile Investments and Finance PLC comes with a heritage of trust, stability and the highest security, giving public the best return for their investments.

Savings

At MI, our savings accounts cater to both minor holders and general savings account holders, advocating the habit of saving within the Sri Lankan economy.

- » Minor Savings Accounts
- » Savings Accounts

Value Added Services

Workshop Services

MI is an attentive partner and as such offers its many credit customers a fully equipped workshop providing motor vehicle repair and servicing facilities.

☑ *G4-DMA, G4-8*

Markets Served

With the on-going expansion of the branch network, MI has widened its presence to target a larger segment of society, to bring financial solutions closer to communities with diverse needs and aspirations. The Company caters to peoples' unfulfilled personal and entrepreneurial need for credit and sound and secure investment opportunities. Our target market includes people that come from all strata of society and our coverage has expanded over the years to cover key economic locations of the country.

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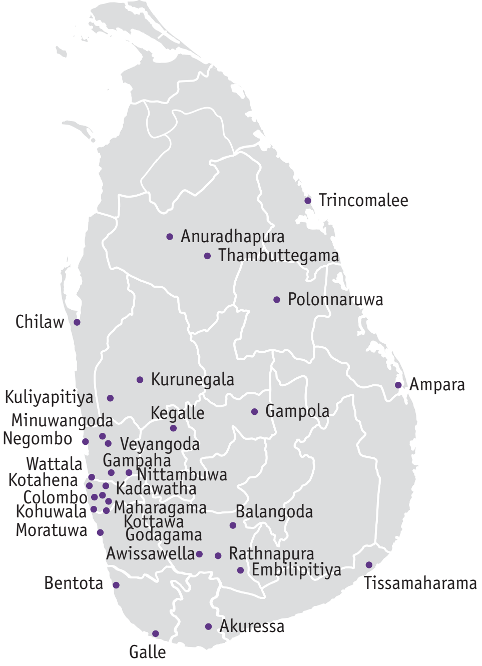

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About Us

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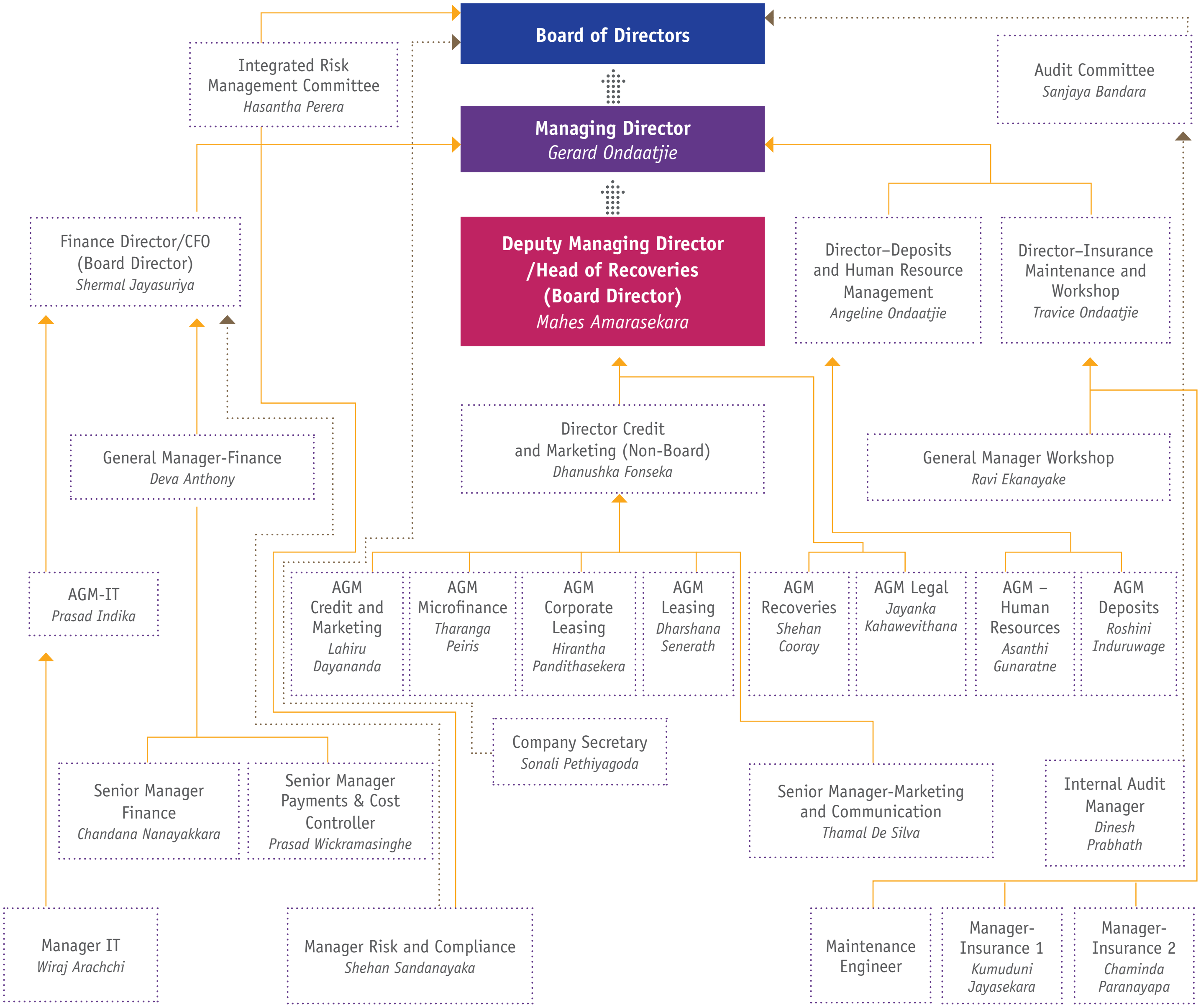
Organisational Makeup

Ownership Structure

The Company is not a subsidiary of any holding entity and has no investments in subsidiaries of its own. However, it holds a 26.12% stake in its associate company, Nuwara Eliya Hotels Company PLC as at the balance sheet date. There were no material changes to MI's organisation size, structure and ownership during the period under review.

Organisational Reporting Structure

The organisational hierarchy depicted below reflects a simple structure, one that facilitates smooth communication flow between each layer of the hierarchy. Job roles of each key designated officer mentioned and their subordinates have been specified based on formal job descriptions.



How we Create Value

Decades of Value Generation

Through a highly successful business enterprise, MI over the last five decades has been a source of strength to all those who have sought our financial services and business acumen. As a Company built on sound fundamentals, our philosophy has always been to give the best in whatever we do and when doing so to retain the trust and loyalty of people, as a true test of our brand promise. In pursuit of our wider aspirations and goals, we operate our own unique business model with embedded value creating processes.

In constantly responding to the opportunities and challenges of our external environment, we have honed our business acumen, knowledge and competencies over time and with it our value enhancing model. Our value creation efforts have benefited all our stakeholders, the industry and the nation over the last fifty plus years.

We have evidenced a continuous increase in wealth for our investors over time; we have been successful in providing the capital required by entrepreneurs in key industries, to customers in pursuit of improving their lifestyles in tandem with the growth of per capita income levels as the country developed from being a closed economy to a mixed economy and to its current status of being a middle income country. As financiers, we have added value to the various initiatives of our customer base with our knowledge and business acumen in guiding their investment decisions and being a supportive and responsible financier who has always ensured regulatory compliance in transacting business. Our strong capital adequacy ratios, governance and risk frameworks have safeguarded the capital of our depositors even in volatile challenging times. The investment returns to our depositors have been guaranteed by our prudent approach and stringent regulatory compliance and adjusted for risk.

As employers we have been known for our commitment to developing careers and creating the opportunities for knowledge development and skill and competency building. Our investment in our employees has gone beyond compensation and reward. We are an employer of choice and earned the coveted position of being among the "Great Places to Work" within a short span. Our strong bonds with our community through our interactions have led to spawning entrepreneurial skills and development of cottage industries which we have supported and nurtured through our business expertise. We have uplifted the less privileged through our corporate philanthropy and corporate social responsibility initiatives that have given us the social license to operate across Sri Lanka over the last fifty plus years as a socially acclaimed responsible corporate citizen.

However, we do not rest on our laurels; as for us, value creation does not end with investor wealth creation, but extends beyond commercial boundaries to touch lives, hearts and minds of people and communities we transact business with, by contributing to their own individual wealth creation and development. Our efforts towards this purpose are further underlined by our continued commitment to reduce our carbon footprint and conserve the environment for future generations.

Value Generating Components

In effectively articulating our value creation story and performance for the concluded financial period, we have structured our report based on various components of the integrated business model we operate. This mainly involves the six forms of input capital that we manage, which is interlinked to our core business activities and back-office support functions. We assessed our internal strengths and weaknesses along with comprehensive review of the external environment and went on to craft suitable strategies that would enable the Company to attain the goals and targets set based on our overarching sustainability agenda. Through our integrated thinking and this value enhancing process, key business processes and sub processes have been interlinked and aligned to generate maximum value, so that we are equipped to cater to the wide ranging stakeholder expectations. As the final output stemming from the model, the process generates our value offering to our customers and in parallel generates number of sustainable outcomes which enhances key stakeholder value, inclusive of contributing to the economic growth endeavours of the country and communities and making every endeavour to conserve the environment and reduce our carbon footprint with a view to preserving the environment and our world for future generations.

Journeying in Integrated Value Creation

Value creation has been a continuous process of perfecting our model as we continue to analyse, revisit and fine tune the components of the model each year. This has resulted in improved business acumen and improvisation of strategy that is a result of the dynamics that prevail in both the internal and external environment in which we operate. More importantly it has also motivated us to aspire for greater heights. The various components, outputs and outcomes of the model have been page referenced in the diagram taking our readers through our unique value creation process. These sections discuss our performance for the year under review in greater detail, and the management actions that led to enhancing the six forms of capital. It also compares current year results with the past year's performance and provides insight into the forecasted performance for 2017/18.

About Us

Our Integrated Business Model

Vision, Mission & Values (32 Page)

Strategic Objectives (69-72 Page)

Capital Inputs

Financial Capital

Represents the pool of funds available for the Company. High interest rates prevailing in Sri Lanka raised the financing costs of MI, and coupled with the below par growth in the loan book led to the realisation of lower Net Interest Income. Balancing short term and long term interests remained challenging given the volatile nature of our business. *(74-93 Page)*

Relationship Capital

The trust we have developed over time has been crucial in facilitating effective relationships with our numerous stakeholders. *(94-115 Page)*

Human Capital

We rely on the skills, well-being and motivation of our employees to generate value. Providing a safe working environment, investing in training and ensuring fair labour practices are regarded as critical in maintaining of an effective labour force. *(116-127 Page)*

Intellectual Capital

The success of our business model is dependent on having the right people, in the right roles, informed by effective management systems and Company culture to build MI brand. Investing in these skills and systems requires sufficient financial capital and will have a positive impact in developing our people and business processes. *(128-133 Page)*

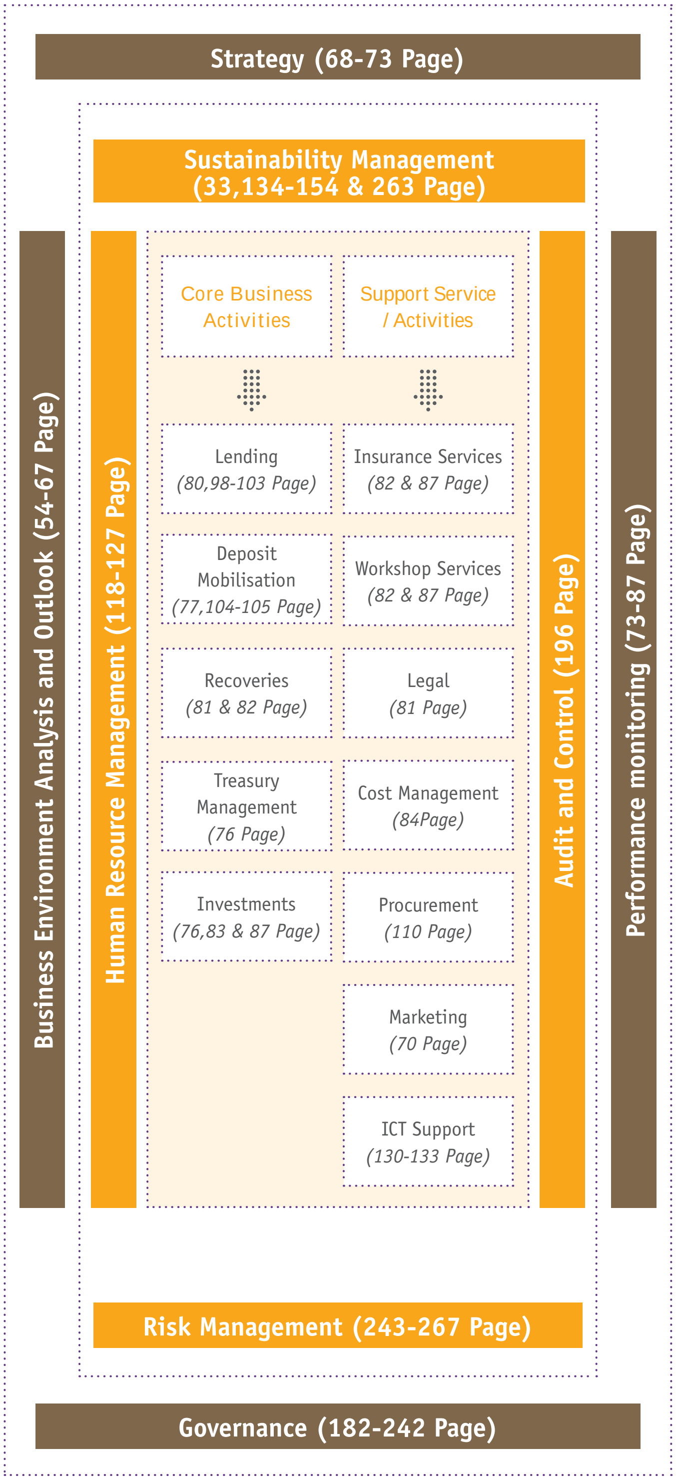
Natural Capital

As an organisation that is expanding, increasing impact to the environment calls for more responsible practices. We navigate our business processes to curtail our carbon footprint and look for ways to protect the fauna and flora. *(134-143 Page)*

Social Capital

The Company over time has developed a reputation for being a socially responsible corporate as demonstrated by our efforts at improving the livelihoods of the underprivileged members within our society. *(144-154 Page)*

Value Creation Process



Strategy (68-73 Page)

Sustainability Management (33,134-154 & 263 Page)

Business Environment Analysis and Outlook (54-67 Page)

Human Resource Management (118-127 Page)

Core Business Activities

- Lending (80,98-103 Page)
- Deposit Mobilisation (77,104-105 Page)
- Recoveries (81 & 82 Page)
- Treasury Management (76 Page)
- Investments (76,83 & 87 Page)

Support Service / Activities

- Insurance Services (82 & 87 Page)
- Workshop Services (82 & 87 Page)
- Legal (81 Page)
- Cost Management (84Page)
- Procurement (110 Page)
- Marketing (70 Page)
- ICT Support (130-133 Page)

Audit and Control (196 Page)

Performance monitoring (73-87 Page)

Risk Management (243-267 Page)

Governance (182-242 Page)

Output

Leases, Hire Purchases, Loans & Advances and Deposits

(98-105 Page)

Carbon Footprint

(141 Page)

Stakeholder

Outcomes

Investors *(111-115 Page)*	Customers *(95-107 Page)*	Employees *(116-127 Page)*	Suppliers/ Lenders *(110 Page)*	Regulatory Bodies *(108-109 Page)*	Society *(144-152 Page)*	Environment *(134-143 Page)*
» Profitability Growth » Dividends » Capital Adequacy » Assets & Liability Mismatch	» Customer Satisfaction » Loyalty/ Retention » Responsible Marketing » Innovation	» Remuneration & Other Benefits » Knowledge Accretion » Enhanced Employee Wealth » Career Advancement	» Sourcing of Funds » Optimal Pricing » Lasting Supplier Relationships » Quality Goods & Services	» Implementation of Rules & Regulations » Accurate Tax Payments » Loan To Value (LTV)	» Community Service » Ethical Business » Social Empowerment	» Green House Emission » Sustainable Green Practices

Six Capital Value Transformation

Impacts

» Stable Returns » Contribution to the Economy	» Financial Empowerment » Brand Loyalty » Total Customer Experience	» Creating Employment » Job Security » Productive Workforce	» Lasting Supplier Bondage » Quality Sourcing	» Contribution to National Development » Prudent Management	» Sustainable Community Development » Responsible Corporate Practices » Supporting National Growth	» Emission Control » Protecting Environment & its Habitats » Sustainable Living

About Us

☑ *G4-18*

Deciding on the Report Content

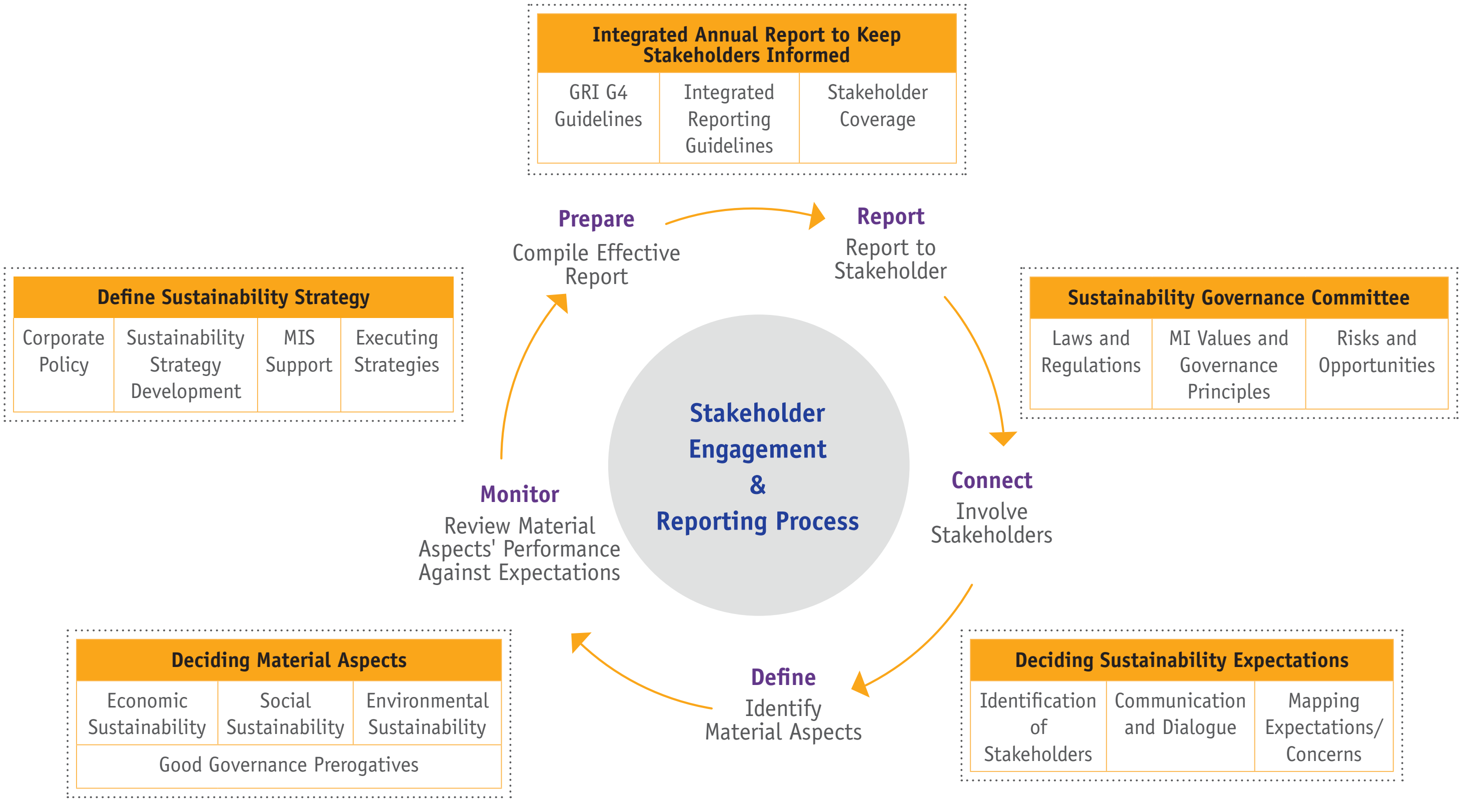
A combined reporting format

We drew on the renowned International Integrated Reporting Council's (IIRC) integrated reporting framework and the Global Reporting Initiative's (GRI) G4 framework to decide on this year's report content and the level of coverage. In doing so, we went on to apply the reporting principles and disclosure guidance of both frameworks. This combined approach, made it possible for us to describe MI's performance for the current year in a concise manner which offers meaningful information to all our stakeholders. We have complied with the key principles of the frameworks on quality, balance, accuracy and reliability of the information reported and also maintained comparability, clarity and timeliness in our reporting.

Approach to Content Selection

The content selection was carried-out through a formal process that involved a five step approach. We obtained first-hand information, views and perceptions of the market and people at large at the commencement of the process through our continuous engagement with all our stakeholder groups. During this process, the Company consulted, interacted and obtained feedback from stakeholders with regard to their expectations of the Company. Through these interactions, the management of MI was able to make an informed decision on matters that were deemed to be of importance to each stakeholder(s) while being important to the viability and long terms sustainability of the organisation. Each topical issue identified and selected through the engagement process was subjected to a materiality test which assisted management in shortlisting the material issues for the reporting period. To ensure effectiveness of the content selection process, it was also essential that we maintained a strong monitoring mechanism, to review key matters identified for reporting and thereafter proceed with the preparation of the Report. Stemming from this review and information extraction process towards compiling this Report, we included an additional section on intellectual capital.

Stakeholder Engagement and Reporting Process



☑ *G4-24 to 27*

Stakeholder Engagement

For the purpose of reporting and maintaining continuous dialogue, as part of our "stakeholder engagement" process, we have selected eight key stakeholders or stakeholder groups that require our attention. Out of this list "our investors" remain the primary stakeholder of the Company while the other stakeholders are also deemed important parties towards the long term sustainability of the organisation as they have an impact and interest in the affairs of the Company.

Key stakeholders and their importance	Engagement methods	Frequency	Material topics/concerns
Investors MI's shareholders are considered the primary stakeholder group. As investors of capital, they require a gamut of financial and non-financial information on MI's performance to gauge the progress made in terms of creating shareholder wealth and to make other assessments on the performance of the Company.	» Shareholder meetings/ Annual General Meeting	» Annual	» Investor returns and performance vis-à-vis KPIs and forecasted targets
	» Annual Report Feedback Form	» Annual	» Company performance
	» Announcements to CSE	» Ad hoc, as necessary (Quarterly Interim accounts)	» Investor information/ MI Performance
	» Extraordinary General Meetings	» Ad hoc, as and when necessary	» Material matters needing investor concurrence
	» One-on-one meetings	» As necessary	» Investor information and relations
	» MI corporate website	» On a regular basis	» Company information
	» Press releases and articles in magazines	» Ad hoc, as necessary	» Company information
Customers Customers who transact with MI remain the next key stakeholder group. Meeting their expectations is vital for MI's long term sustainability.	» Direct customer feedback at MI's service points/suggestion boxes	» On a regular basis	» Customer needs, suggestions and complaints
	» Marketing visits/ Field visits	» Credit customers - mostly once prior to transacting » Deposit customers – on an ad hoc basis and selective	» Product information and customer evaluations » Product information and customer Support
	» One-on-one meetings	» As necessary	» Customer relations and complaint resolution
	» Telephone discussions / E-mails	» On a regular basis	» Quality of service
	» Media campaigns	» On a regular basis	» Product awareness
	» MI corporate website	» On a regular basis	» Product information

About Us

Key stakeholders and their importance	Engagement methods	Frequency	Material topics/concerns
Employees MI’s employees play an integral role in MI’s continued success and their impact to MI”s performance and achievements of goals and their aspirations, needs and concerns are of paramount importance.	» Departmental review meetings	» Monthly	» Operational Performance Versus rewards and recognition
	» The “open door policy ” for employees to freely interact one-on-one with the MD, other Directors of the Board and senior officers.	» On a regular basis	» Employee suggestions/ grievances
	» Management meetings	» Weekly	» Business performance
	» Performance appraisal and individual review meetings	» Bi annual	» Appraising of employee performance
	» Internal newsletter communiqués	» Annual	» MI and industry information
	» Corporate communiqués through circulars, memos and e-mails	» Regular	» Operational information/compliance
	» Company social events including get-togethers, sports day, other celebrations and religious events	» MI Get-together -Annual » Other events – ad hoc	» Social informal relations » Team building and social relationships
Regulators Being in a highly regulated industry and as a listed public company, MI is subject to regulation and assessments by regulatory bodies. To ensure compliance with regulatory and statutory requirements and their timely implementation and due to the need to obtain assistance and advice, regulators are considered an important stakeholder.	» On-site and off-site reviews by CBSL and other regulatory bodies	» Annual	» To assess the degree of regulatory compliance
	» Other discussions with the Board and senior management	» On a regular basis	» Regulations/compliance review
	» Issue of regulations and requirements by regulators	» As necessary	» Regulations/compliance review
	» Submission of returns and status reports	» As necessary	» Carry out compliance reviews on a periodic basis and provide feedback to the organisation
	» Training programs/ workshops with regulatory bodies	» Based on periodic deadlines - weekly to annual	» Extract industry specific information towards developing industry based KPIs and assessment of industry specific progress Regulatory information
	» Submission of special reports	» As necessary	» Compliance review

Key stakeholders and their importance	Engagement methods	Frequency	Material topics/concerns
Suppliers The expanding operations require constant supply of stationary and other consumable items of good quality from reputed suppliers.	» One-on-one meetings	» As necessary	» Supplier performance
	» Routine telephone discussions	» On a regular basis	» Product/fund sourcing
Lenders MI's banking partners are an important component of MI's business, as they support the Company in meeting its immediate and long term funding needs. A lasting relationship is therefore essential to maintain continuous funding, that is mutually beneficial.	» Periodic visits undertaken by either party	» As necessary, usually once a year with key parties	» Supplier relations
	» Review of performance and status according to agreements entered into	» As necessary	» Supplier review » Financial information of prior periods and forecasts for performance evaluation » Industry reports
Society/Local Community With the expanding presence of the Company, MI's interaction continues to increase with various communities. It is important to understand the wants of people and to identify ways of fulfilling them, while sustaining future business for the Company, towards building mutually beneficial sustainable relationships with society.	» Interacting with segments of society by direct correspondence and meetings.	» To commence and implement a projects	» Financial inclusion
	» Conducting islandwide surveys	» Annually	» Social grievances/wants
	» Communicating with society through press releases and through reporting	» As necessary other than annual reporting	» Societal information
Environmental Groups As MI continues to widen its branch network, it becomes important for the Company to ensure that its business operation does not hamper the environment, deplete scarce/natural resources and negatively impact the surrounding environment.	» Using the widening branch network to interact with local communities	» As necessary	» Social dialogue
	» Public events and sponsorships	» As necessary	» Public relations and awareness
	» Sustainability website	» On a regular basis	» Sustainability information

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☑ *G4-17 to 21*

Topic Identification and Aspect Boundary

The topics selected for reporting this year were selected as an outcome of the stakeholder engagement process, the application of materiality testing and the final topic selection undertaken in keeping with IIRC's integrated reporting framework and the Global Reporting Initiative's (GRI) G4 framework. Accordingly, we conformed to the GRI G4 reporting framework and guidelines and considered all other regulatory and voluntary reporting requirements, which were incorporated in to the integrated reporting structure, adopted this year. Topics deemed important from the point of view of the Company as well as from the stakeholders' perspective were listed down and were subject to a "materiality test".

After listing down the topics, we decided on the materiality of the impact the respective issues would have on either the organisation or/and its stakeholders and also from the perspective of sustainability. For each identified aspect in each topic, we decided on the impact level by marking them as either high,medium or low. Aspects of lesser importance were filtered out and not reported on, to ensure relevance based on materiality. For each identified aspect, the applicable "boundary" was evaluated, on whether it impacted the stakeholders internally or externally, in order that a proper assessment of the matters was carried out depending on the probable impacts and their materiality.

G4 Aspect	**Materiality Level of Aspect (High/Medium/Low)**			**Aspect Boundary**							**Reporting Status**	
				Internal	**External**							
	Impact on Mercantile Investments	**Impact to MI Stakeholders**	**Impacts in terms of MI's Sustainability Context**	**MI Head Office, Branches and Employees**	**Investors**	**Customer**	**Suppliers**	**Lenders**	**Society/ Environment**	**Regulators**	**Reported**	**Not Reported**
Economic												
1. Economic performance	High	High	High	✓	✓	✓		✓		✓	✓	
2. Market presence	High	High	High	✓	✓	✓					✓	
3. Indirect economic impact	Medium	High	High						✓		✓	
4. Procurement practices (including borrowing of funds)	Low	Medium	Medium				✓	✓			✓	
Environment												
5. Materials	Low	Low	Medium				✓		✓		✓	
6. Energy	Medium	Low	Medium						✓		✓	
7. Water	Medium	Low	Medium						✓		✓	
8. Biodiversity	Low	Medium	Medium						✓		✓	
9. Emissions	Low	Medium	Medium						✓		✓	
10. Effluents and waste	Low	Low	Medium						✓		✓	
11. Products and services	Low	Medium	Medium						✓		✓	
12. Compliance	Low	Medium	Medium						✓	✓	✓	
13. Transport	Medium	Medium	Medium						✓		✓	
14. Overall	Medium	Medium	Medium						✓		✓	
15. Supplier environment assessment	Low	Low	Medium				✓		✓		✓	
16. Environment grievance mechanisms	Medium	Low	Medium						✓		✓	
Social : Labour Practices and Decent Work												
17. Employment	High	High	High	✓							✓	
18. Labour/management relations	High	High	High	✓							✓	

G4 Aspect	Materiality Level of Aspect (High/Medium/Low)			Aspect Boundary							Reporting Status	
				Internal	External							
	Impact on Mercantile Investments	Impact to MI Stakeholders	Impacts in terms of MI's Sustainability Context	MI Head Office, Branches and Employees	Investors	Customer	Suppliers	Lenders	Society/ Environment	Regulators	Reported	Not Reported
19. Occupational health and safety	High	High	High	✓							✓	
20. Training and education	High	High	High	✓							✓	
21. Diversity and equal opportunity	High	High	High	✓							✓	
22. Equal remuneration for women and men	High	High	High	✓							✓	
23. Supplier assessment for labour practices	Low	Low	Low									✓
24. Labour practices grievance mechanisms	High	High	High	✓							✓	
Social : Human Rights												
25. Investment	Medium	Low	Low	✓							✓	
26. Non-discrimination	High	High	High	✓							✓	
27. Freedom of association and collective bargaining	Low	Low	Low									✓
28. Child labour	High	High	High	✓							✓	
29. Forced or compulsory labour	High	High	High	✓							✓	
30. Security practices	High	High	Medium	✓							✓	
31. Indigenous rights	Low	Low	Low						✓			✓
32. Assessment	High	High	High	✓	✓	✓	✓				✓	
33. Supplier human rights assessment	Low	Low	Low									✓
34. Human rights grievance mechanisms	High	High	High	✓	✓	✓	✓	✓	✓		✓	
Social: Society												
35. Local communities	High	High	High						✓		✓	
36. Anti-Corruption	High	High	High						✓		✓	
37. Public policy	Low	Low	Low									✓
38. Anti-competitive behaviour	Low	Low	Low						✓			✓
39. Compliance	High	High	High						✓	✓	✓	
40. Supplier assessment for impacts on society	Low	Low	Low						✓			✓
41. Grievance mechanisms for impacts on society	Low	High	Medium						✓		✓	
Social: Product Responsibility												
42. Customer health and safety	High	High	Medium			✓		✓			✓	
43. Product and service labelling	High	High	High		✓	✓		✓			✓	
44. Marketing communication	High	High	High		✓	✓		✓			✓	
45. Customer privacy	High	High	High		✓	✓		✓			✓	
46. Compliance	High	High	High		✓	✓		✓		✓	✓	
Sector Specific Disclosure - Society:												
47. Access points to disadvantaged	Medium	High	Medium			✓				✓	✓	
48. Financial services to disadvantaged	Medium	High	Medium		✓	✓				✓	✓	

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G4 Aspect	Materiality Level of Aspect (High/Medium/Low)			Aspect Boundary							Reporting Status	
				Internal	External							
	Impact on Mercantile Investments	Impact to MI Stakeholders	Impacts in terms of MI's Sustainability Context	MI Head Office, Branches and Employees	Investors	Customer	Suppliers	Lenders	Society/ Environment	Regulators	Reported	Not Reported
Sector Specific Disclosure – Product Responsibility:												
49. Portfolio of business lines (FS6)	High	High	High			✓					✓	
50. Products and services with social benefit (FS 7)	Medium	High	Medium		✓	✓					✓	
51. Products and services with environmental benefit (FS8)	Medium	Medium	High						✓		✓	
52. Audit coverage to assess implementation of environmental and social policies and procedures	Medium	Medium	High						✓		✓	
53. Active ownership (FS 10 and FS 11)	Low	Low	Low						✓			✓

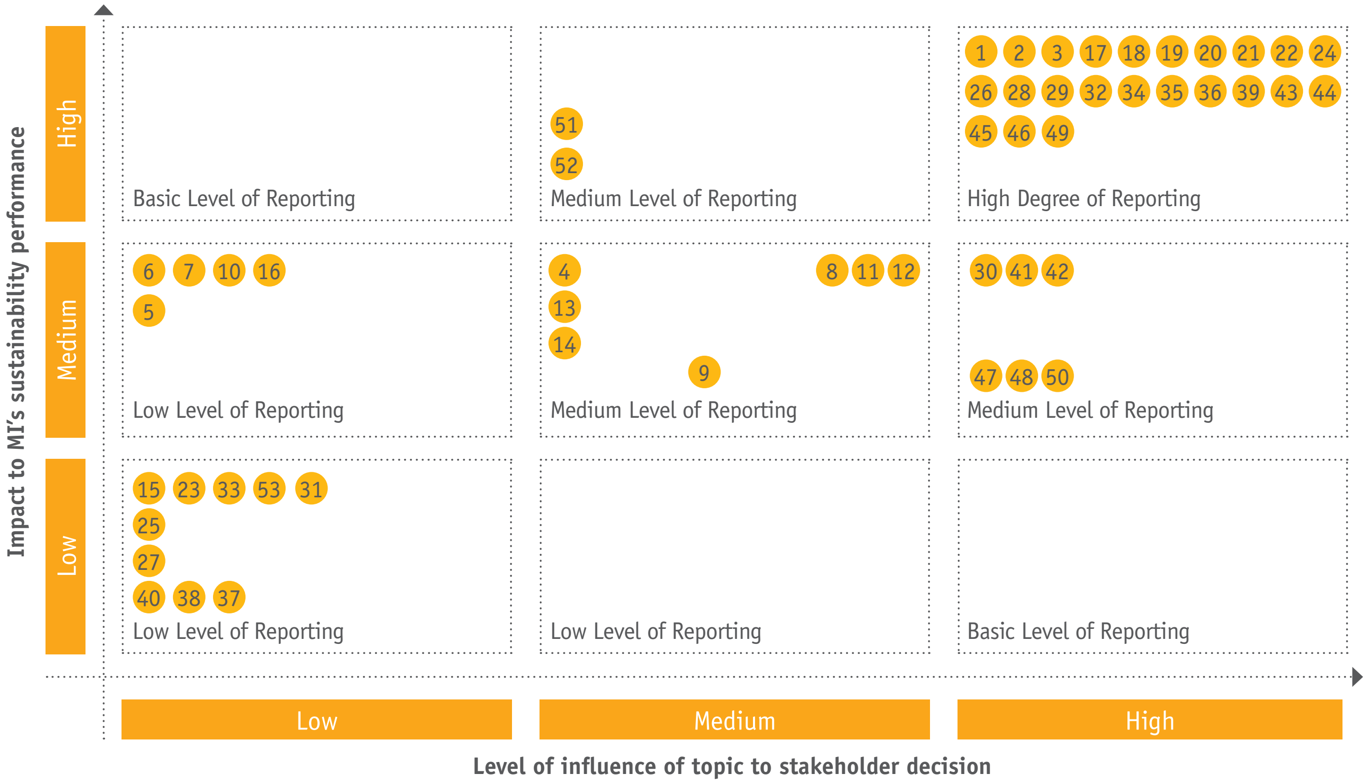
Aspects not reported with reasons for exclusion

G4 Aspect /Sector Specific Aspect or Indicator	Materiality Level of Aspect (High/Medium/Low)			Reasons for Exclusion from Reporting
	Impact on Mercantile Investments	Impact to MI Stakeholders	Impacts in terms of MI's Sustainability Context	
Social : Labour Practices and Decent Work				
23. Supplier assessment for labour practices	Low	Low	Low	Our Finance business does not involved major materials supplier participation except for the supplying of inventory vehicles, stationary and consumables deemed immaterial when compared against the main operation of the Company.
Social : Human Rights				
27. Freedom of association and collective bargaining	Low	Low	Low	No trade union exist within the Company and there is harmonious relationship between management and employees with clear open door policy.
31. Indigenous rights	Low	Low	Low	Being a service organisation, there is minimal interaction of our operations with environment and habitats.
33. Supplier human rights assessment	Low	Low	Low	Our Finance business does not involve supplier participation except for the supplying of inventory vehicles, stationary and consumables deemed immaterial when compared against the main operation of the Company.
Social: Society				
37. Public policy	Low	Low	Low	As a quoted independent organisation with no interaction with public bodies other than normal course of transactions, public policy considerations are not deemed as material aspects for reporting.
38. Anti-competitive behaviour	Low	Low	Low	As an organization that does not resort to any anti-competitive behaviour, considerations under this aspect are deemed immaterial to report.
40. Supplier assessment for impacts on society	Low	Low	Low	Our Finance business does not involve major material supplier participation except for the supplying of inventory vehicles, stationary and consumables deemed immaterial when compared against the main operation of the Company.
Social: Product Responsibility				
53. Active ownership (FS 10 and FS 11)	Low	Low	Low	The Company assessed that there is no significant direct impact to society or environmental harm arising from our business as we only deal in financial transactions.

The "Materiality Gauge Matrix" given below summarises all key topics short listed during the materiality testing phase and highlights the reporting extent of each topic. Detailed reporting was adopted for aspects identified as high impact, in terms of the level of influence the aspect posed to stakeholder decisions and to MI's sustainability performance. In the event the aspect did not have a materially significant impact on the stakeholders and MI's sustainable performance such aspects were eliminated for further reporting or not reported upon extensively. This approach ensured that the overall content of the report is precise and provides only the required disclosures in relation to material aspects. In keeping to the GRIs' G4 Comprehensive reporting framework, all required indicators relating to the identified material aspects have been reported on, together with the required specific standard disclosure for the finance sector, if considered as material.

Further, we have provided a list of aspects that are not material and not reported on in the current year's Report along with the rationale for exclusion.

Materiality Gauge Matrix



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Key Stakeholder Impacts

Our business operations and other supporting activities impact our stakeholders in numerous ways once again this year. The most important impacts remained positive with fewer negative impacts over last year. In-depth disclosure pertaining to material topics associated with each key stakeholder has been covered under each form of Capital in the Management Discussion and Analysis as page referenced below.

MI's Key Stakeholders	Key Impacts to the Stakeholder in 2016/17			
	Key Positive Impacts	**Key Negative Impacts**	**Section Highlighting Detailed Impacts**	**Page No.**
Investors	» Generated investor wealth, posting steady profitability. » Increased net worth of the Company.	» The Rate of return generated for capital invested, remained lower than what was planned on account of lower core margins and impairment provisions.	» Financial Capital » Relationship Capital (Investors) » Intellectual capital	74 to 93 111 to 115 128 to 133
Customers	» Through MI's expanded business operation we extended credit facilities to a large number of customers, making funding freely accessible.	» Our lending rates were increased in tandem with increasing market interest rates which curtailed lending to certain price sensitive segments.	» Relationship Capital (Customers) » Financial Capital	95 to 105 87 to 93
Employees	» A more skilled and knowledgeable workforce led to better productivity. » Reward and recognition of performance led to motivated employees who were able to excel in their chosen fields due to being empowered.	» The construction of a separate building that would cater to additional parking, recreational facilities along with an in-house gym did not materialise this year. Instead, as an immediate requirement, commenced the construction of a large staff lunch room at the Head Office premises.	» Human Capital	116 to 127
Regulators	» Made necessary changes operationally to cater to new regulations imposed. » Maintained close coordination with all regulatory bodies and sought advice and clarifications as and when necessary.	» As anticipated, share prices did not increase to expectation in 2016/17, and could not dispose the balance excess investment component, to keep in line with the Investment Direction issued by CBSL. However, as given in Note No. 22 in the Financial Statements, MI was able to dispose the excess investment after the year end.	» Relationship Capital (Regulators)	108 & 109

MI's Key Stakeholders	Key Impacts to the Stakeholder in 2016/17			
	Key Positive Impacts	Key Negative Impacts	Section Highlighting Detailed Impacts	Page No.
Suppliers/ Lenders	» Registered additional suppliers for consumable goods. » Recruited a procurement executive and increased focus on procurement and supplier relationship building. » The treasury division was able to negotiate attractive rates and strengthen relationships with key lenders and funding agencies.	» Could not secure funding from overseas investment partners as planned. The domestic cost still remained relatively cheaper than overseas sourcing for the Company.	» Relationship Capital (Suppliers/ Lenders)	110
Society/Local Community	» Assisted the poor and the low income earners, extending funding to individuals to financially empower them, to better their standards of living. » Went beyond commercial boundaries to assist the poor and lesser privileged providing them with better shelter, educational support, medicine, etc., through our CSR initiatives.	» Received suggestions and recommendations to increase our social support from members of society. Some of the matters could not be addressed this year and will be looked at next financial year.	» Social Capital	144 to 152
Environmental Groups	» Through the green initiatives and environmental conservation projects that were initiated, we contributed by planting trees in Bathalagoda Wewa in Kurunegala and took steps to assist injured wild animals in coordination with local authorities, to be initiated next financial year.		» Natural Capital	134 to 143

Management Discussion and Analysis

pro•gres•sive

adjective

1. *happening or developing gradually or in stages; proceeding step by step*

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2. *favouring or implementing new, liberal ideas*

Synonyms

1. continuing, increasing. 2. growing, developing. 3. ongoing.

Management Discussion and Analysis

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Management Discussion and Analysis

CFO's Statement on Performance

"Our financial progress remains a constant journey OF IMPROVEMENT for us... AS IT CONTINUES to empower all those within the Company IN CREATING AND ENHANCING stakeholder value over time"

Our Financial Solidity

It was a challenging year for the Non-Banking and Financial Institutions, mainly due to the persistent rise in interest rates which continued to exert pressure on the cost of funding, core-margins and eventually pegged back chances of posting higher levels of profitability. Nevertheless, overall financial performance for the year ending 2016/17 was steady but remained constricted due to high impairment charges, but was mainly driven by the satisfactory revenues derived, from steady lending volumes; core business spreads and cost optimisation initiatives that were achieved for the period under review. The results are satisfactory given the challenging external environment and the numerous regulatory revisions made during the year. We consolidated our business presence in key locations, integrating our business strategy and operational activities to create investor wealth to a reasonable degree. Our financial progress remains a constant journey of improvement for us... as it continues to empower all those within the Company in creating and enhancing stakeholder value over time.

Through focused leadership, the corporate management and staff were closely guided by the Board to pursue challenging financial targets and operational goals. As the Finance Director and CFO overseeing the finance function, I wish to recognise the efforts of the treasury division who made a significant contribution to the overall performance of the Company through the sourcing of cost effective funding and careful matching of assets and liabilities, contributing immensely in easing the growing pressure exerted on core business margins. I believe MI's financial solidity will be further cemented as we continue to consolidate our position at branch level, expanding our reach and customer base over the duration of the foreseeable future.

Excellence in Financial Reporting

I reiterate MI's commitment to excellence in corporate reporting, adhering to international reporting frameworks such as the Global Reporting Initiative (GRI G4) and the Integrated Reporting Framework. We have been successful in articulating the Company's integrated business processes which include the sustainable value creation for key stakeholders. The Company was recognised yet again at number of events for its excellence in financial reporting in producing a world-class Annual Report. While being recognised locally at the CA Sri Lanka, and CMA Institute Annual Report Awards, it was similarly pleasing to obtain international recognition, winning three other awards at the Arc Awards ceremony held in New York.

Outlook for Financial Prospects

In keeping to the medium term strategic plan, we hope to achieve the optimistic growth targets set out in 2015. The future outlook appears positive especially considering the uptick witnessed in economic activity, which augurs well for the Financial Services Sector, which is in search of new ways of boosting revenue and profitability. While the industry dynamics look quite challenging, I believe there remains enough opportunity in the market specially in non-traditional lending for the industry to achieve the anticipated turnovers, and to generate a reasonable return for its investors. Financially, MI will expect to see a growth of its fund base from its increased presence and acquisition of new customers with interest income being a key driver of both revenue and profitability leading to strengthening its capital position further, to reach over 18% prudential capital adequacy levels. Our investments in improving our operating platform will support the growth and profitability objectives of the Company.

Shermal Jayasuriya
Finance Director/CFO

12th September 2017

Management Discussion and Analysis

Business Environment Analysis

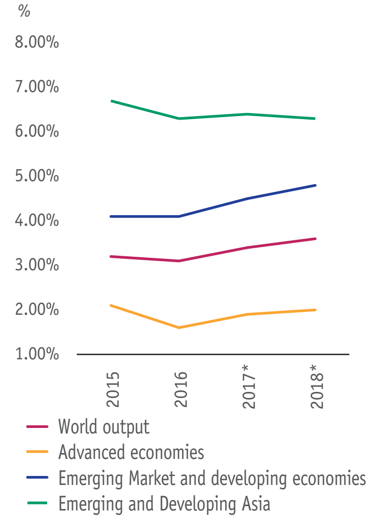
World/Sri Lankan/Industry/MI Growth Trajectory

	FY 2015/16	FY 2016/17	Expected – FY 2017/18
World Economic Growth	3.20%	3.10%	> 3%
Sri Lanka Real GDP Growth	4.80%	4.40%	> 4 %
LFC/SLC Sector Asset Growth	22.30%	21.70%	> 15%
MI Asset Growth	20%	10.00%	>10%

Global Economic Landscape

Global output remained stable mostly driven by the pick-up witnessed in advanced economies in the second half of 2016, but the growth dipped marginally to 3.1%, down 0.1% from a year before. Based on the International Monitory Fund (IMF) World Economic Outlook (WEO) update 2017, however, in contrast emerging market economies slowed down than expected, mostly reflecting unique factors. Despite challenges facing the global markets and the lacklustre out-turn in 2016, economic activity is projected to pick up pace in 2017 and 2018, especially in emerging markets and developing economies. Nonetheless, the policy stance of the incoming US administration and its global ramifications would be quite telling, and is bound to impact Emerging and Developing Asia due to their stance on trade, labour practices, etc., and also the changing US domestic interest rates and turnaround in stock prices, that is bound to somewhat peg-back FDI flow into Sri Lanka. The dominance of China as a growing economic force, and India's widening role on the international front has shaped the Asian region as a key economic region. In this context, it is essential that our nation continues to nurture close ties with our Asian neighbours and obtain the support of the international community to generate better flow of FDI's and exploit international trade opportunities in favour of the country.

World Economic Growth Trajectory



* *Projected*
Source: IMF World Economic update 2017

Global Economic Impact to Finance Business

Modest foreign exchange reserves and the inability to attract greater flow of FDIs, continued to weaken the rupee against the dollar by 4% in 2016, based on the calendar end exchange rate. This has a direct impact on the already pricey vehicle importation cost that tended to rise further, thus, pegging back demand for brand new vehicles and reconditioned vehicle financing backed imports. Moreover, the noticeable slowdown in foreign investor participation in the capital markets contributed to the lacklustre stock market performance, which negatively impacted the fair values of MI's large equity portfolio. Nonetheless, the improving global sentiments of Sri Lanka and the Government's policy and initiatives in boosting domestic and international trade continued to drive the domestic economy, propelling most sectors including the finance industry. Pick up in tourism and trade, and the start-up of partnerships with China and foreign investors continued to fuel the domestic economy, sustaining steady demand for credit and fresh opportunities for the LFC sector.

Sri Lankan Economy

The Sri Lankan economy remained resilient in 2016 despite uncertainty and volatility, but showed signs of stability in the midst of sound actions by the Government and the Central Bank. The economy in 2016 grew at a relatively slower rate of 4.4% in real terms compared to 4.8% recorded in the previous calendar year. Other than the global economic ill effects, domestic events such as unfavourable weather conditions caused the Sri Lankan economic growth to slow down. On a positive note, tightened fiscal and monetary policies and increased investment expenditure, especially in the construction sector, drove economic growth during the year. From a finance industry perspective, the upward movement in interest rates and government taxes, and regulations restricting credit growth were the main challenges observed for the period while the exchange rate devaluation and inflationary effects took a secondary role. However, the finance industry was able to thrive on the economic development activities commenced since the cessation of hostilities, and the growing demand for credit stimulated particularly as a result of the development emerging in the industry and service sectors. Increasing wealth of high net worth individuals and growing income levels of the middle income earners driven by their growth in earnings and the sound employment levels recorded again this year, paved the way for the greater mobilisation of deposits for finance companies.

Financial Sector Performance **

The financial sector continued to expand during the year whilst exhibiting resilience amidst challenging market conditions, both globally and on the domestic front. The growth of the sector was buoyed by the expansion in banking, other deposit taking financial institutions and contractual savings institutions.

Along with the expansion, the stability of the financial system was maintained without causing major macro-prudential concerns in an environment of supportive regulatory measures for stability.

Performance of Licensed Finance Companies (LFC's) and Specialised Leasing Companies (SLC's)

The LFCs/SLCs sector recorded a strong performance in terms of asset growth and branch expansion, whilst placing emphasis on gradually moving out from its core business of vehicle financing to other loan products. By end 2016, this sector comprised of 46 LFCs and 7 SLCs and 1,313 branches reflecting an 8% increase in branch total from a year before.

» Assets and Liabilities of the sector

Total assets exceeded the trillion rupee mark expanding by 21.7% to Rs. 1,211.9 Billion albeit growth was slower paced than prior year's growth of 22.3%. Lending activities remained the main source of asset growth, which accelerated by 21% to Rs. 962.7 Billion, lower than the high of 31.8% growth recorded in 2015. In terms of the liability composition, the overall funding structure of the sector showed a shift from deposits to borrowings as seen in the last two years, considering the flexibility and cost factor. Borrowings increased by 39.6% while deposits recorded a moderate growth of 10.5% compared to a 16.1% growth recorded in 2015.

MI's Performance against LFC Sector

Steady loan book growth, drove MI's total assets up by 10%, but remained lower than the industry average of 21.70% recorded for 2016, as we adopted a risk aversive strategy. Nevertheless, MI's interest income growth remained at similar levels as the industry which showed an above 20% growth year-on-year.

However, the impact of rising interest rates and the re-pricing effect impacted MI's earnings, which is being addressed through focused strategies to improve core margins. Based on the shorter term profile of MI's deposit base, MI's funding cost moved up more rapidly than lending yields, but the pressure exerted on margins will ease once higher yield based strategies and cost control measures takes effect.

MI's tier 1 and total risk weighted capital adequacy ratios were above 14%, well over the prudential regulations and also the industry average. This enabled MI to be on a better financial footing, to face inherent industry risk which is deemed relatively higher than the banking sector.

Composition of Assets and Liabilities of LFC and SLC vs MI

Item	Actual Overall 31-Dec-2016 Rs Billion(a)	Actual Overall 31-Dec-2015 Rs Billion(a)	MI's Actual 31-Dec-16 (as a % of Sector item)
Assets			
Accommodation	962.7	796	2.91
Finance Leasing	490	419	2.26
Hire Purchase	42	73	14.98
Investments	111.7	100	5.15
Others	137.5	101	0.18
Liabilities			
Total Deposits	531	481	3.12
Total Borrowings	438.7	314	2.46
Capital Elements	146.1	123	5.58
Total Funds	1,115.8	918	3.18
Others	96.2	78	1.14
Total Assets/ Liabilities	1,212	996	3.06

Management Discussion and Analysis

Financial Sector Performance **

» Industry Risks Factors

Amidst the growth in portfolio, the quality of lending was maintained due to aggressive credit recovery policy. Hence, the NPL ratio declined from 5.7% in the last calendar year to 5.3 % in 2016.

Liquidity levels remained at satisfactory levels amidst increased lending activities. However, with the market interest rates increasing, the sectors exposure to the "re-pricing risk" was high, reducing sector margin due to prevailing negative assets and liability mismatches.

» Profitability

Greater expansion of lending business, paved the way for the sector to record a higher post-tax profit of Rs. 31.5 Billion compared to Rs. 15.2 Billion recorded in 2015. The net interest income of the sector nevertheless slowed down to 12% while the net interest margin dipped to 7.9% from 8.7% recorded in 2015, mostly on account of the re-pricing effect increasing cost of funding.

» Capital Position

The total regulatory capital improved by 25.1% to Rs. 116.2 Billion mainly due to retained profits. Except for few companies operating below the minimum required capital levels, others maintained capital adequacy ratios. The core capital and total risk weighted capital ratios increased to 11.4% and 11.7% respectively.

MI's Performance against LFC Sector

Composition of Income and Expenses of LFC and SLC Sector vs MI

Item	Actual Overall 31-Dec-2016 Rs Billion(a)	Actual Overall 31 Dec-2015 Rs Billion(a)	MI's Actual 31-Dec-16 (as a % of Sector item)
Interest Income	188.9	150.4	2.64
Interest Expense	96.8	68.2	2.88
Net Interest Income	92.1	82.2	2.39
Non-Interest Income	28.3	22.8	1.07
Non-Interest Expense	65.6	67	2.33
Loan loss Provisions (Net)	7.6	9.5	3.87
Profit Before Tax	47.2	28.5	1.35
Tax	15.7	13.3	1.56
Profit After Tax	31.5	15.2	1.24

Source: The Annual Report of Central Bank of Sri Lanka 2016

Outlook

Regulations issued in 2017 to raise core capital levels of NBFI's on a staggered basis to Rs. 2.5 Billion will entail smaller LFC's to merge with larger ones, if adequate capital cannot be brought in. This, however, will not impact MI as its capital base is well over the minimum future requirements.

However, as a result of the continued upward rise in lending interest rates impacting borrower repayment capacity, MI would be cognizant of the pressure exerted on maintaining asset quality. To minimise impairment charges against profitability, a focused recovery drive will be continued with to sustain healthy collection levels.

In the midst of market volatility, and controls placed over credit growth, we expect profitability levels to be somewhat held back, but is bound to pick up once credit growth picks up and interest rates start to reverse on a downward trend.

Other impacts to MI resulting from key economic changes in variables and trends can be outlined as follows;

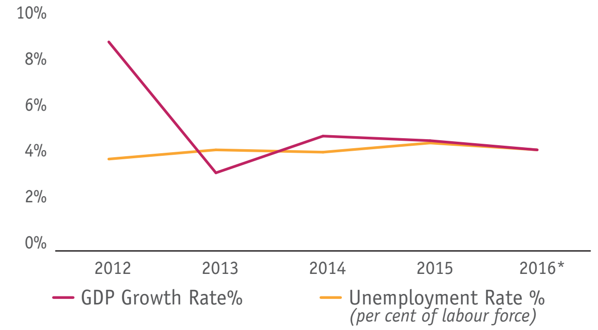
Movements in Key Domestic Economic Variables in 2016**

Sri Lankan Economic Growth

Sri Lankan economic growth in real terms stood at 4.4% declining by 8% from last year, but remained resilient in the midst of domestic and external factors.

- Economic growth was supported by the recommencement of few large projects that included the Port City project and buoyant private sector investment activities. However, apart from the negative impacts stemming from global economic changes in performance and sentiments, the growth momentum was pegged back due to the continuation of fiscal consolidation measures to enhance Government revenue, inflationary pressure increasing towards the latter part of 2016 and weather conditions affecting output.
- Unemployment stood at 4.4% down 6% year-on-year, but shortage of skilled labour and the lower representation of women in the labour force remained a constraint in expanding the economy.
- Moreover, uncertainty that arose from frequent policy changes impacted the economic growth momentum, causing volatility in demand for goods and services and general business outlook and sentiments towards the stock market.

GDP Growth Rate & Unemployment Rate



** Provisional*

Source : CBSL Annual Report 2016

Sri Lankan Economic Impact to MI

By closely monitoring the development taking place at regional level, we aligned our core business plans to capitalise on regions that had higher levels of economic activity and town development underway. We improved the operating platform and increased cadre in branches reporting higher performance levels and also by expanding the branch network in locations that were attractive in terms of economic activity and per capita income distribution.

The pick-up in tourism and continued high performance of the industry sector, particularly the construction industry increased demand for our leases, corporate loans, personal loans and property mortgage. Micro funding needs of the lower income earners was another key segment pursued. However, based on sector credit risk evaluations, we were cautious in our lending to specific sectors such as agriculture, but increased business more into the transport sector which remained lucrative.

We were also successful in mobilising higher levels of fixed deposits beyond the Western Province, taking note of the increasing wealth amongst the lower and middle classes, and the per capita incomes closing in on the 4,000 US dollar mark.

Management Discussion and Analysis

Movements in Key Domestic Economic Variables in 2016**

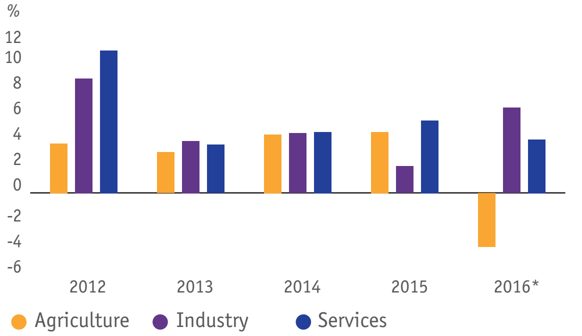
Sectorial Performance

On the basis of production estimates, growth was mainly driven by expansion in industry and services related activities while a contraction was recorded in agriculture due to adverse weather conditions. The agriculture sector contracted by 4.2% as opposed to a 4.8% growth recorded in the last calendar year.

Encouragingly, the value added by the industry sector recorded a significant growth of 6.7% in 2016 compared to just 2.1 % growth recorded in 2015. The industry activities which comprise of construction, mining and quarrying, manufacturing, electricity, water and waste treatment activities were key drivers of the sector.

Service related economic activity which collectively account for the major share of the Gross Domestic Product (GDP), expanded by 4.2% but remained relatively slower paced compared to a 5.7% growth posted in 2015 in value added terms. Financial services and transportation sectors significantly supported the growth momentum in this sector.

Annual Sectorial Growth



** Provisional*
Source : CBSL Annual Report 2016

GDP and the Per Capita

GDP at current market prices was estimated at Rs. 11,839 Billion up by 8.1% from last year, largely attributable to the upturn in GDP implicit deflator which increased to 3.6% in 2016. The GDP per capita was estimated at Rs. 558,363 in 2016 growing by 6.9% supported by the increase in nominal GDP. However, the per capita GDP in US dollar terms marginally decreased to 3,835 mainly due to the weakening of the local rupee against the dollar.

Sri Lankan Economic Impact to MI

Outlook

Based on an optimistic national GDP and per capita income growth forecast, we expect to further consolidate our position in active locations and will complete plans on decentralising the total deposit operation to widen our reach through branch deposit mobilisation. We hope to maintain asset quality by following a risk based approach to lending, and this will entail majority of disbursements be directed towards lower and viable middle level risk sectors.

Movements in Key Domestic Economic Variables in 2016**

Inflation

The Colombo Consumers' Price Index (CCPI, 2006/07=100) annual average rose to 3.7% in 2016 from just 0.9% last year while the CCPI YOY period end was up at 4.1% compared to 2.8% recorded a year before.

» The general price level, as measured in terms of the movements in both National Consumer Price Index and Colombo Consumers' Price Index, followed an overall increasing trend, with mixed movements during 2016.

» The movement of the general price level was largely in line with the price movements of the food category. Tax adjustments introduced to non-food category also triggered upward movement in general price levels.

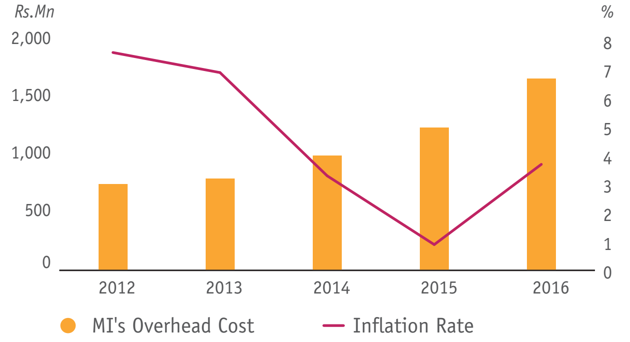
» Price increases in the world market coupled with the weakening of the domestic currency fuelled increases in prices of imported goods, exerting further pressure on domestic prices.

» Wages increased in nominal terms across all sectors of the economy although real wage erosion was observed in the public and formal private sectors. Two major Acts on the National Minimum Wage and the Budgetary Relief Allowance which were introduced, propelled the nominal wages of employees in the private sector.

Sri Lankan Economic Impact to MI

MI's overhead cost escalated partly due to inflationary factors, but was up mainly because of increased business operations.

Inflation Last Five Years vs MI's Overhead Cost Movement



Source:CBSL CCPI (2006/07=100) Annual Average

Inflationary factors also continued to impact savings of the masses, but were not severe as inflation remained at single digit. There was no direct noticeable impact to the demand for credit, but the core-relation prevailing between inflation and interest rates was another contributory factor that drove market interest rates upward, exerting pressure on core margins enjoyed by the Company.

Outlook

To improve future profitability levels, there will be greater emphasis placed by MI on cost optimisation. With the implementation of the new externally purchased international ICT system, our processors and procedures will be enhanced further, thus easing dependence on the human element, forcing resultant cost to be lowered.

Monetary Policy Stance

The Central Bank tightened its monetary policy stance restraining excessive growth of monetary and credit aggregates, to contain demand driven inflationary pressures in the economy.

The lending and deposit rates of the Company were revised at numerous times, based on continued upward movement in market interest rates, to afford attractive and competitive pricing. As a consequence, our core margins continued to be pressured due to the re-pricing effect where deposit cost increased at a relatively faster pace than the lending yields. Bank borrowings also remained expensive as the year progressed, ultimately moving up and evening out at similar costs to the deposit cost levels.

Management Discussion and Analysis

Movements in Key Domestic Economic Variables in 2016**

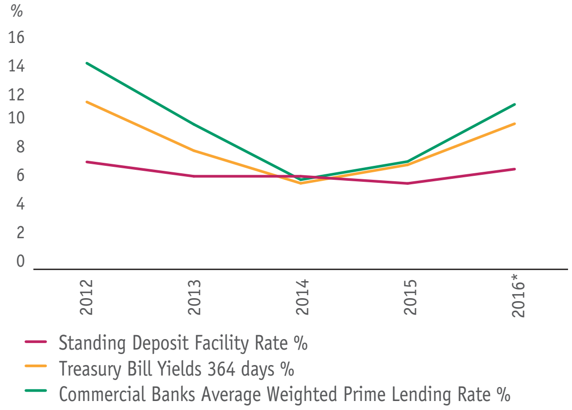
Credit Growth

Rupee liquidity in the money market, which was in surplus during the first quarter of 2016, turned to a deficit thereafter, before increasing toward end 2016. To absorb excess liquidity and manage inflationary pressures, the Statutory Reserve Ratio (SRR) applicable on Licensed Commercial Banks was raised by 1.50% to 7.50% while the key policy interest rates, namely the Standing Deposit Facility Rate and the Standing Lending Facility Rate were increased by 50 basis points. The expansion of private sector credit decelerated to 21.9% by end 2016 from a peak of 28.5% mid 2016, but the deceleration was somewhat below expectations.

Interest Rates

Yields on Government securities showed an upward trend despite some moderation observed in the second half of 2016. Increased demand for funds by the government and impacts of monetary tightening drove yields upward in the treasury bill market and longer tenor Government securities. A significant increase in deposit rates by both the LFC sector and Banks was reported, manly driven by the aggressive deposit campaigns. Accordingly, the Average Weighted New Fixed Deposit Rate, based on new time deposit rates of Commercial Banks rose significantly 431 basis points to 11.44% by end 2016. Similarly, lending rates were also increased due to rising cost of funding on account of the high deposit rates. As a result, the Average Weighted Prime Lending Rate (AWPLR) notably increased by 399 basis points to 11.52% from 7.53% recorded in 2015.

Market Interest Rates

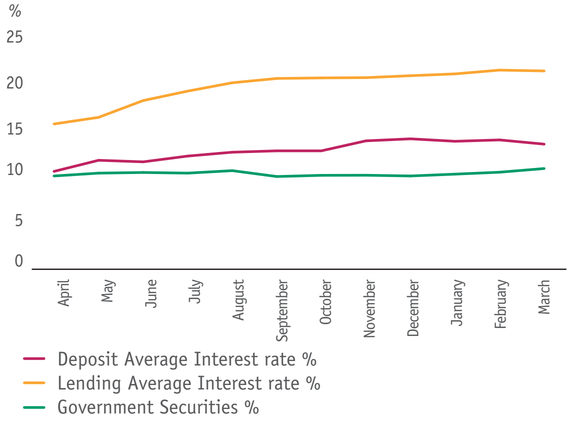


Provisional

Source : CBSL Annual Report 2016

Sri Lankan Economic Impact to MI

MI Deposit and Lending Average Interest Rate Averages vs Government Securities One Year



Outlook

We expect the upward movement in interest rates to ease and later on reverse in the medium term, which will immediately improve core spreads for the industry. In the interim, MI will capitalise on its high yielding lending products to increase average yields and look for cheaper funding sources to improve core margins.

Movements in Key Domestic Economic Variables in 2016**

Fiscal Policy

The Government committed to implementing revenue based fiscal measures, recognising the persistently low revenue mobilisation in the past that led to high budget deficits and fiscal imbalances.

Measures were taken to simplify the tax structure while broadening the tax base. Tax administration was also strengthened through the automation of tax collecting agencies with the implementation of the RAMIS project.

A revised VAT rate of 15% was brought about after approval of the parliament in 2016 while a simplified single corporate income tax rate of 17.5% was proposed for all sectors other than a few sectors including the banking and financial services sector for which a rate of 28% would be applied and 40% tax rate for liquor and other specified basket of items. Some of the tax proposals put forward including the income tax rate upward revisions are still in the proposal stage and yet to be introduced.

How the vehicle sales market was impacted

The high duty structure for motor vehicle imports continued to draw considerable amount of revenue for the government but remained a stumbling block for the vehicle sales market and the LFC's in increasing financing support for brand new and reconditioned vehicles. The vehicle sales market was further impacted, with stricter regulations being imposed during the financial year to curb motor vehicle ownership and financing by reducing the loan to value maximum limit for motor cars to 50% and other additional LTV ceilings for various vehicle categories.

Sri Lankan Economic Impact to MI

With the exclusion of VAT on leases in 2015, MI's lease financing continued to be the preferred product compared to hire purchase financing. However, high import duty structure on vehicles continued to hinder growth in the vehicle sales market, thus pegging back demand for vehicle backed credit. Over and above this, an increased VAT rate of 15% on financial services was applicable from this financial year, further burdening the already high effective total corporate taxes percentage which stood above 40%.

Outlook

To counter prevailing impediments to the vehicle backed lending, MI will pursue consolidating its position at branch level, to generate volume growth focusing on developing the potential non-traditional lending market. Emphasis will be placed on identifying credit opportunities in addition to vehicle based lending.

Management Discussion and Analysis

Movements in Key Domestic Economic Variables in 2016**

Colombo Stock Exchange (CSE) Performance

Colombo Stock Exchange (CSE) recorded a dismal performance in 2016 for the second consecutive year with the All Share Price Index and the S & P Sri Lanka 20 Index falling 9.7% and 3.6% respectively.

The upward trend in interest rates in both domestic and international markets and the depreciation of the Sri Lankan rupee were some of the factors affecting the market performance. As a result, price indices pertaining to main sub-sectors, namely banks, finance and insurance, diversified holdings, hotels and travels, and telecommunication declined substantially by 7.7%, 16.4%, 7.4% and 12.5% respectively.

Share Market Performance	2015	2016
All Share Price Index	6,894.5	6,228.3
Year-on-Year Change (%)	(5.5)	(9.7)
S & P Sri Lanka 20 Index	3,625.7	3,496.4
Year-on-Year Change (%)	(11.3)	(3.6)
Market Capitalisation (Rs. Billion)	2,938.0	2,745.4
As a Percentage of GDP (%)	26.8	23.2
Market Price Earnings Ratio	18.0	12.4
Average Daily Turnover (Rs. Million)	1,059.6	737.2
Value of shares traded (Rs. Billion)	253.3	176.9
Number of Companies Listed	294	295
Number of Rights Issued	15	6
Initial Public Offers/Offers for sale	27	20

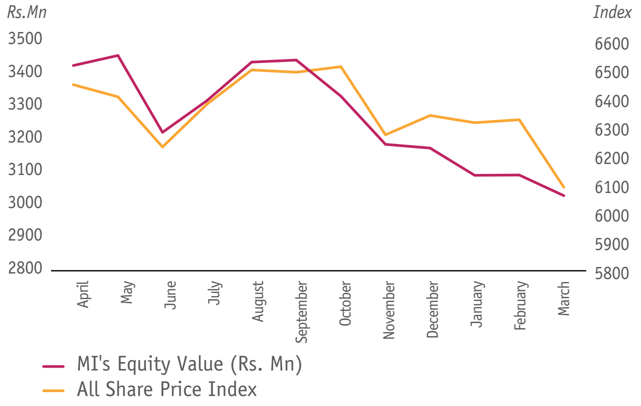
Source: Colombo Stock Exchange

*** Main Source of information: The Annual Report of 2016 of Central Bank of Sri Lanka*

Sri Lankan Economic Impact to MI

Despite the optimism in the leisure and banking sectors, MI's high equity investments in these potential sectors and other sectors such as telecommunication etc., did not perform as expected, with share prices remaining below par, brought down by the continued sluggish market conditions.

MI's Equity Value Monthly vs All Share Price Index



Source: Colombo Stock Exchange

Outlook

Increasing foreign participation in the stock market during 2017, boosted by the improving international sentiments, should drive the stock market upward gradually. In the short term nevertheless, the proposed economic changes brought about by the new US administration would have negative impacts on the Asian region with anticipated FDI outflows.

Our Strengths and Weaknesses

As part of the strategic planning process, we reviewed our internal capabilities identifying the following as our key strengths and weaknesses. This assessment helped us map out the approach and actions required to enhance the value of each form of capital, capitalising on our strengths while negating areas of weakness.

Key Strengths Nurtured

Key MI Strengths	How we Leveraged our Strengths in FY 2016/17
MI's unblemished track record and reputation as a successful finance company for over five decades, having a strong capital base that exceeds Rs. 7 Billion as at 31st March 2017.	» We maximised the use of capital and fund availability that helped boost profitability and total capital, while keeping profit retention levels high. » We leveraged on our integrity and financial strength to access low cost funding and drive deposit mobilisation. » Based on our brand identity, financial integrity and unblemished track record, we were successful in attracting new customers and thus widened our customer base, creating new and rewarding relationships with both individuals and corporates alike. Total lending and deposit customers increased 36% and 6% respectively.
Accumulated business knowledge and know how embedded in the business from a successful business model that has surpassed the 50 year milestone.	» Continued to strengthen our existing governance and risk management with increased oversight and risk analysis initiatives to identify and mitigate against emerging risk and drive performance based on prudence. » Acquired new talent and invested in training the total workforce in technical areas as well as providing knowledge and soft skills. » Initiated actions to enhance ICT systems while pursuing a full system migration that is planned to be completed in the next financial year, with a view to aligning our IT strategy with our business strategy.
Possessing an over 800 skilled workforce, with a blend of both young and experienced professionals.	» Further strengthened the workforce through recruitment, managing to attract talented individuals to take up key positions bringing in new insights and thinking to the business. » Inculcated a learning culture and empowered employees to remain motivated and creative in their jobs, recognising top performers and those contributing to the efficiency of operations.
Strong branch network with over thirty business locations across the country.	» Through a more decentralised approach and marketing drive, catered to a wider market disbursing 83% credit from the branch network and managing to mobilise 13% as new deposits from the network. » Made radical changes to certain operational practices, and procedures for purpose of reducing operational lead-times, making transaction handling convenient and efficient resulting in an improved end-to-end customer experience and improved productivity.

Key Weaknesses Countered

Key MI Weaknesses	How we Countered Weaknesses in FY 2016/17
MI's traditional lease and hire purchase financing being the main contributor to revenue.	» The overarching lending strategy focused on two important factors of increasing volume and yields. » We were successful in developing our term based lending product range to boost volumes and yields while promoting traditional lending through lease and hire purchase offerings.
Mobilisation of fixed deposits remains the main deposit product with over 90% contribution.	» Introduced need based convenient modes of transacting including payments, to promote MI savings and kids saver deposits. » Plans are also underway to provide ATM facilities from next financial year, to attract higher levels of savings deposits towards improving the deposit mix.
Based on the nature of business, lending is carried out for relatively longer periods than deposits mobilised, leading to funding mismatches in the less than one year tenures.	» Despite the tendency for deposits to be placed more in the short-term, we also mobilised longer term fixed deposits to control short term assets and liability mismatches. » Secured one year and above borrowing facilities to further bring down mismatches.

Management Discussion and Analysis

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Key Risks, Challenges and Opportunities

Economic/Business Impacts

Key Risks/ Challenges/ Opportunities	**Impacts to LFC Sector/Sustainability Impacts**		**How MI Approached Economic/Business Impacts in FY 2016/'17**	**Future Outlook on Impacts**
	Positive Impacts	**Negative Impacts**		
LFC industry sophistication, competitiveness and widening regulations.	» Wider customer choice for financial products. » Tight regulation and monitoring ensures sector stability.	» Growing direct and indirect competition from within and outside the industry. » Rise in interest rates, currency devaluation and regulatory changes slowed already high credit growth, increased funding cost and overheads.	» Based on the three year strategic plan, we developed a wider product range offering financial solutions which were needs based and improved our reach by expanding our branch network across the country. » Implemented effective business strategy to ensure core business margins are maintained at a sustainable level. » Continuous training and development which increased training hours per employee from 19.53 to 44.8. » The corporate governance framework was revised and reinforced with sound risk identification and management measures, comprehensive legal support, more oversight through audit and compliance.	The Finance industry credit growth is expected to slow down in the short term but should pick up as witnessed in previous years. The competition and increased regulation will remain high and therefore we can expect greater diversification and innovation to take place and drive the industry.
Credit growth restrictions, high import duty and depreciation in local currency pegged back the vehicle market.	» Increased demand for non-vehicle backed credit.	» Deceleration in demand for lease and hire purchases. » Deterioration in asset quality when moving away from more secure forms of lending.	» In combination with traditional financing, developed other products -personal loans, corporate loans, property mortgages and microfinance credit lines during the year. » Strong asset quality measures were put in place to cut down on default risk. » Strengthened the special recoveries task force, and maintained steady collection levels and regularised overdue and problematic customer accounts. » The internal valuation unit was active in determining more realistic and accurate valuations and also was able to dispose repossessed vehicles;	While brand new vehicle imports remained sluggish, registered market motor vehicle demand will pick up. The industry will cater to more non-traditional lending unlike in the past, to fund the SME sector, ventures, projects, etc., that are bound to arise, as the economy progresses.

	FY 2016/17	**FY 2015/16**
Number of internal valuations carried out	8,484	6,861
Repossessed vehicles sold during the period	159	332

Key Risks/ Challenges/ Opportunities	Impacts to LFC Sector/Sustainability Impacts		How MI Approached Economic/Business Impacts in FY 2016/'17	Future Outlook on Impacts
	Positive Impacts	Negative Impacts		
Advancement in technology and changing customer preferences.	» Easy access to technology based devices enables customers to better evaluate the market. » Those receptive to changes in customer preferences, were able to improve their operating platforms to meet with customer expectations and needs.	» Customer price sensitivity impacted core margins. » High investment in technology is a critical success factor requiring the involvement of management input and posing constraints on management time in crossing the technology chasm.	» Advertising and promotion campaigns which included social media coverage were initiated to build sound customer awareness. » Offered a personalised customer service with attractive rates for deposits that included special promotional rates and special rates for senior citizens. » Engaged the services of an ICT consultant, and drew up an ICT strategy to enhance ICT system capabilities to support future technological needs of the business and align with the business strategy.	Technology will play a significant role in shaping the future of the industry. ICT advancements will drive new business opportunities for the sector. The industry expects to compete on an equal footing with the banking sector. It is envisaged that the industry will invest more in enhancing ICT infrastructure in the next few years.
Expanding business operations in a climate of economic revival and volatility.	» Greater business opportunities for those having increased presence. » Increasing need for credit beyond Western Province, from the middle and lower income earners.	» Market volatility and challenges within the financial services sector impacted asset quality. » Escalating overhead costs due to operational expansion and inflationary factors.	» The expansion drive that picked up pace during the last five years decelerated as greater focus was placed on leveraging of existing MI locations. » Tailored products to fit customer budgets and made necessary rescheduling of facilities for borrowers in difficulty, to ease repayments. » Appointed a cost controller to closely review cost elements and their escalations, to recommended cost control measures and cost optimisation.	Despite the expected economic growth, we can expect branch expansion activities to slowdown, unlike in the past. More consolidation is bound to take place, focusing on higher revenue generation from existing infrastructure and facilities.

Management Discussion and Analysis

Social Impacts

<table>
<tr><th rowspan="2">Key Risks/ Challenges/ Opportunities</th><th colspan="2">Impacts to LFC sector/Sustainability Impacts</th><th rowspan="2">How MI Approached Social Impacts in 2016/’17</th><th rowspan="2">Future Outlook on Impacts</th></tr>
<tr><th>Positive Impacts</th><th>Negative Impacts</th></tr>
<tr><td>In a competitive environment, managing and retaining key talent in the workforce will be perceived as challenging.</td><td>» Capacity constraints faced from non-availability of adequately skilled and experienced workforce to meet with modern day challenges of the finance business.
» Locally hired individuals being more familiar with respective community.
» Meeting the employment needs of the Millennials.</td><td>» Retention of skilled employees who are equipped to deal with the rapidly changing industrial conditions would become increasingly difficult.
» Work-life balance would be threatened by the high expectations and performance driven culture prevalent in organisations.
» Challenges posed from managing the needs and expectations of a high performing workforce.</td><td>» Promoted top performers and also made following new recruitments;
<table><tr><th>Gender</th><th>2016/17</th><th>2015/16</th></tr><tr><td>Male</td><td>250</td><td>222</td></tr><tr><td>Female</td><td>52</td><td>42</td></tr><tr><td>Total</td><td>302</td><td>264</td></tr></table>» Adopted an employee-centric approach, sustaining motivation and morale in driving productivity. The number of training hours to staff increased by 129% and instilled a clear performance based reward system, taking a goal oriented stance.
» Recruitment from local communities stood at 70%.</td><td>In a constantly changing dynamic business environment, nurturing and retaining the right calibre of staff will not be easy. The planned increased decentralisation in MI’s operation will entail greater investment in people management, resulting in improved communication, empowerment and leadership development.</td></tr>
<tr><td>Improving per capita income and the savings habit of the various economic strata in society.</td><td>» Creation of greater demand for luxury items including motor vehicles.
» This stimulates economic development, fuelling demand for credit to fund consumption.</td><td></td><td>» Refocused and carried out campaigns to mobilise deposits from individuals residing in key parts of the country.
» Offered a variety of credit alternatives that included financing, personal loans, vehicle loans, etc., to varying customer segments.</td><td>With the expected acceleration of economic activity, national GDP and per capita income is bound to increase over time. Most industries including the finance sector will benefit from this in the future, with increasing demand for luxury items and widening opportunity for business start-ups, etc.
MI’s long term strategy is geared to harness these anticipated economic developments and future opportunities.</td></tr>
</table>

Key Risks/ Challenges/ Opportunities	Impacts to LFC sector/Sustainability Impacts		How MI Approached Social Impacts in 2016/'17	Future Outlook on Impacts
	Positive Impacts	Negative Impacts		
Societal needs beyond commercial boundaries are many, and mostly remain uncatered.	» The industry is in a better footing to cater to the wants and unmet or partially met needs of people, as there is a better reach.	» There is no immediate benefit to corporates in fulfilling non-commercial based social needs. » Corporates, who are insensitive to societal needs, will not obtain a social license to operate among the various communities.	» MI's growing branch network catered to the varying credit and investment needs of a large cross section of society. » The microfinancing unit was able to cater to a large segment of customers with its small ticket lending.	The gap between the haves and the have nots will remain wide and will take time to bridge. Some of the basic necessities of the poor will remain uncatered to, and hence the business community will be asked to play a key role in alleviating poverty, more so than in the past.

Product	Customers served outside Western Province			
	FY 2016/17 Number	FY 2016/17 Value Rs. Million	FY 2015/16 Number	FY 2015/16 Value Rs. Million
Lending	22,524	6,517	13,399	6,070
Fixed Deposits	294	490	220	197

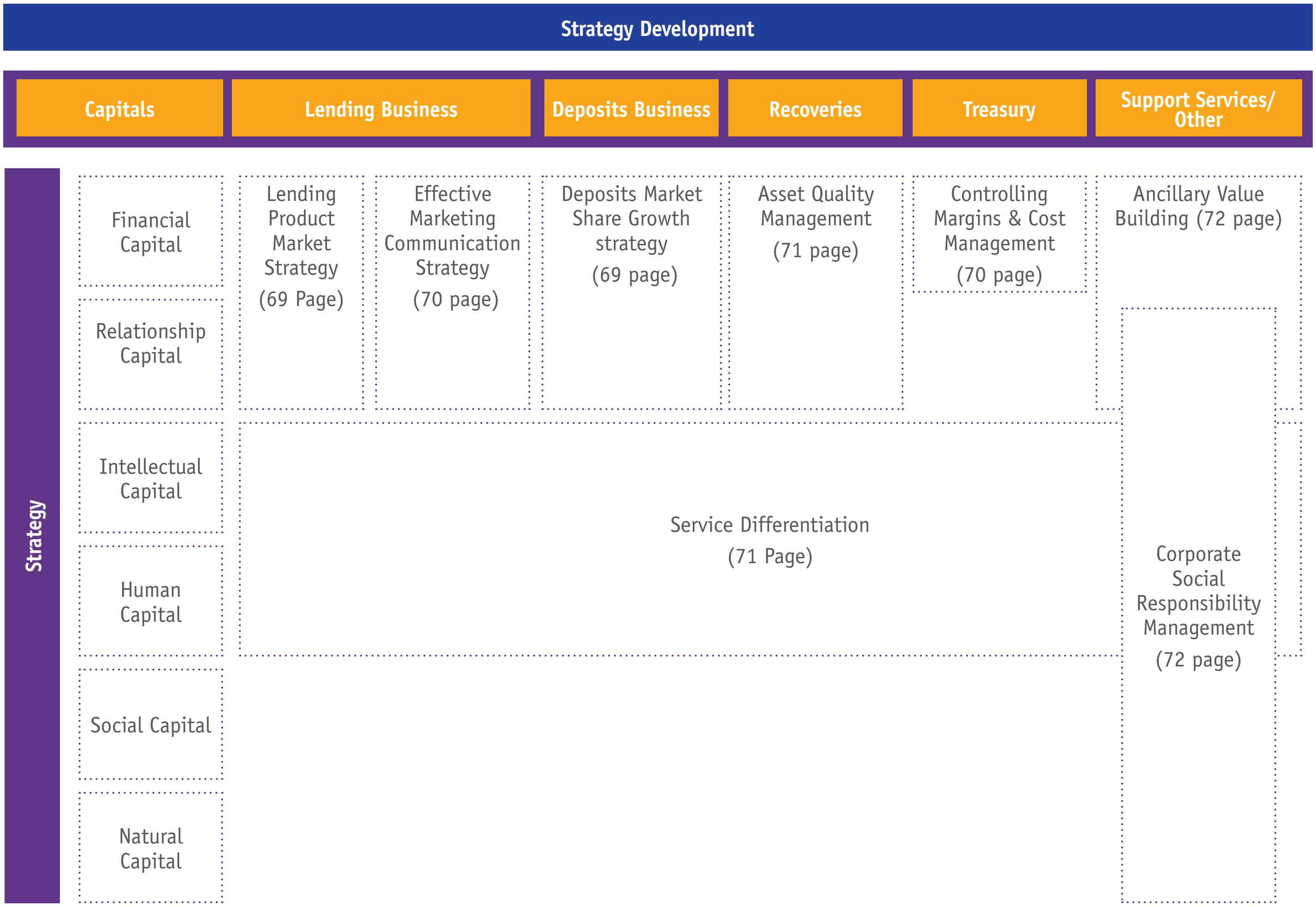
Environment Impacts

Key Risks/ Challenges/ Opportunities	Impacts to LFC Sector/Sustainability Impacts		How MI Approached Environment Impacts in 2016/17	Future Outlook on Impacts
	Positive Impacts	Negative Impacts		
Business expansion requires greater focus on preserving the environment and the continued safeguard of depleting resources.	» Corporates that practice environmentally supporting actions are recognised socially, leading to long term benefits. » Sparring use of resources, through reuse and recycling will eventually reduce related cost.	» Corporate actions negative to the environment would erode brand value and damage reputation. » Branch expansion results in an automatic increase in consumption of natural resources which calls for its greater conservation, preservation and reducing the carbon footprint.	» Ensured sparring use of resources through in house green initiatives. » Implemented effective waste management practices as explained under "natural capital" section. » Controlled total green-house gas emissions which stood at 2,447 tonnes of CO_2. Initiated environmental supportive projects such as the tree planting campaign.	With the increased footprint, LFC's will be required to embrace more environmental-friendly solutions to carry out business. Automation would drive further changes when corporates would move away from the costly brick and mortar concept of a physical presence with the onset of e-commerce, online payment gateways, online platforms and mobile wallet transactions. Large telcos and retailers would provide transaction services which were provided by the financial services sector hitherto.

Management Discussion and Analysis

Strategy and Resource Allocation

The review and evaluation of the internal and external environment led to the identification of our strengths and weaknesses, we also identified opportunities and zeroed in on possible challenges and risks faced by the Company from its external environment. Based on these assessments and banking on the know-how and experience we possess, we devised a combination of strategies, to meet our immediate short term objectives and also pursue long term corporate goals. We displayed our commitment to the primary strategies that we devised, allocating necessary resources for its effective implementation. This paved the way for the organization to stay competitive and to achieve sustainable growth in its sphere of business and at the same time deliver anticipated assistance towards building a more sustainable society.



Strategy Development

Capitals | **Lending Business** | **Deposits Business** | **Recoveries** | **Treasury** | **Support Services/ Other**

Strategy

Financial Capital

Relationship Capital

Intellectual Capital

Human Capital

Social Capital

Natural Capital

Lending Product Market Strategy (69 Page)

Effective Marketing Communication Strategy (70 page)

Deposits Market Share Growth strategy (69 page)

Asset Quality Management (71 page)

Controlling Margins & Cost Management (70 page)

Ancillary Value Building (72 page)

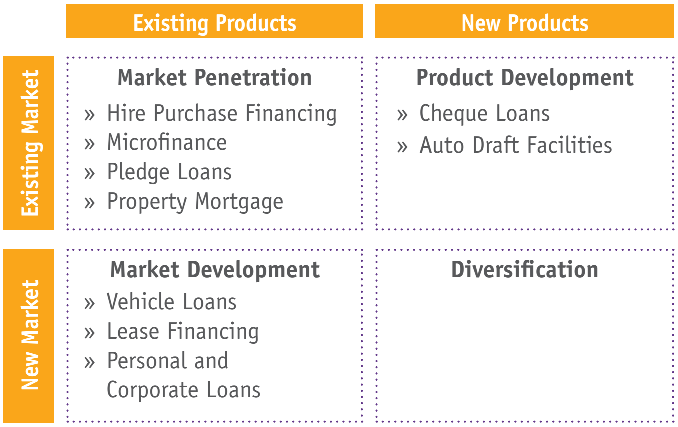
Service Differentiation (71 Page)

Corporate Social Responsibility Management (72 page)

Our Strategy and Resources

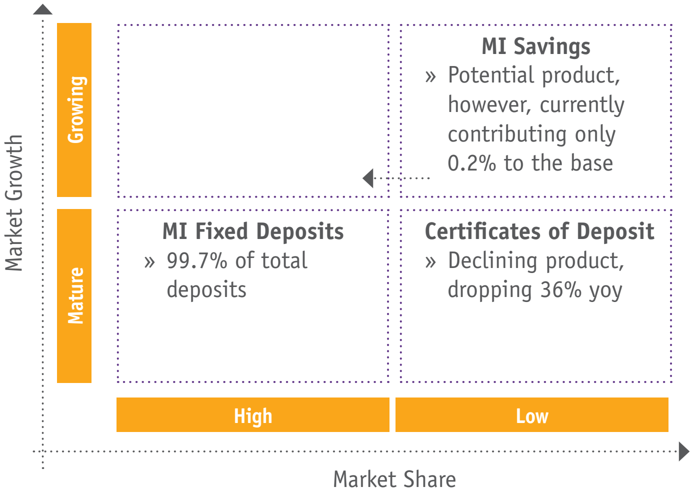
Internal and External Business Analysis Outcomes	Strategic Objective	Strategy	Overview of strategy	Resource Inputs
» Loan to Value (LTV) limitations imposed restricting credit granted against motor vehicle purchases. E.g. The LTV percentage being dropped systematically on motor cars, being a key security category for MI, from 90% to 70% and then to 50% in January 2017. » High import taxes and duty structures on vehicle imports. » Increased industry competitiveness and increased banking sector focus on LFC sector products. » Limited product range and market penetration. » Changing customer perspectives.	**Short Term Objectives:** » Increase lending revenue by 20% from microfinance lending and other high yield lending. » Increase Deposit Mobilisation by 15% to fund credit operation. **Medium to Long Term Objectives:** » Increase Market share from existing 2.66% to 3%. » Increase customer base by 10% by attracting fresh clientele and keeping retention ratio above 70%	**Market Strategy for Lending** ***Refer Diagram 1*** **Rational for Strategy:** To compensate expected impact to revenue from credit restrictions and also to meet higher optimistic revenue targets, it was necessary that we capitalised on our vibrant products such as leases, microfinance and other viable products being offered in the market, to boost revenue. **Market Strategy for Growth in Deposits** ***Refer Diagram 2*** **Rational for Strategy:** While Certificate of Deposits remains a dying product, fixed deposit mobilisation is vital for continuous funding support. However, to sustain long term viability, low cost savings mobilisation is required concurrently.	» Penetrative consolidation strategy within existing markets, adopting differentiation tactics. Highlighting MI's service quality and reputation, carrying out marketing drives in all viable regional hubs. » Identification of new markets, to build vehicle financing, vehicle loans and personal and corporate loan products. » Introduction of new products such as auto drafts and cheque loans to existing markets. » Expanding reach and strengthening branch fixed deposit mobilisation, and in parallel developing the ICT backbone and operational procedures to decentralise operations to boost savings.	» Investment to boost branch operational capabilities and to build brand awareness. » The use of automation for data mining techniques and improving the quality of management information generated. » Investing in market studies and surveys. **Effects on Capitals** » Revenue growth and low cost funding increased profitability and overall Financial Capital – Refer pages 78 to 80 » Increased customer base and loyalty continued to enhance our Relationship Capital– Refer pages 94 to 115

Diagram 1 - Product Market Lending Strategy



	Existing Products	New Products
Existing Market	**Market Penetration** » Hire Purchase Financing » Microfinance » Pledge Loans » Property Mortgage	**Product Development** » Cheque Loans » Auto Draft Facilities
New Market	**Market Development** » Vehicle Loans » Lease Financing » Personal and Corporate Loans	**Diversification**

Diagram 2 - Capturing Deposit Market Share and Growing Deposit Base



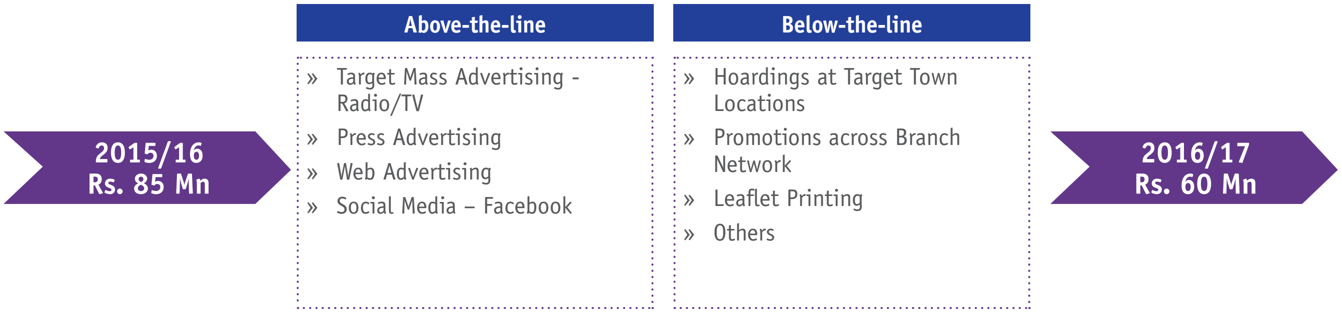
	High	Low
Growing		**MI Savings** » Potential product, however, currently contributing only 0.2% to the base
Mature	**MI Fixed Deposits** » 99.7% of total deposits	**Certificates of Deposit** » Declining product, dropping 36% yoy

Management Discussion and Analysis

Our Strategy and Resources (Contd.)

Internal and External Business Analysis Outcomes	Strategic Objective	Strategy	Overview of Strategy	Resource Inputs
» Competitiveness has led to price sensitivity. » Thinning margins due to rise in interest rates and re-pricing effect. » Escalating operational cost structures due to expansion.	**Short Term Objectives:** » Maintaining Core margins above minimum internal threshold of 8%. **Medium to Long Term Objectives:** » Maintaining cost to income ratio below 55%. » Investment in brand.	**Controlling Margins and Cost Management** **Rationale for Strategy:** » As there is pressure on margins, accessing cheaper sources of funding remained vital for long term success. » Expansion has led to escalating costs that needs close scrutiny and control to cut down wastage.	» Attract cheaper funding from the banking sector and other alternative sources. Ensure adequate capitalisation and compliance with capital adequacy measures. » Monitor routine overhead expenditure, cost optimisation and elimination of wastage. » Effective supplier management.	» Broad base MIS support through ICT enhancements. » Increased human resource hours on revamping purchasing procedures, cost scrutiny and MIS. » Work towards increases in ROA from existing branch infrastructure. **Effects on Capitals** Improving core margins and promoting a more cost conscious culture that focussed on cost optimisation and control. Well-controlled overhead cost structure contributed to profitability and financial capital generation. – Refer Financial Capital on pages 74 to 84 for details.
» Majority of MI's branch network is fairly new. » Many brands in the market, thus requiring brand differentiation.	**Short Term Objectives:** » Attracting new business and consolidating newly set up regions. **Medium to Long Term Objectives:** » Increase market share in lending and deposit mobilisation to 4%.	**Marketing Communication Strategy** ***Refer Diagram 3*** **Rationale for Strategy:** Due to the recent establishment of operations in most locations, awareness about MI's services has still not completely reached some of the local communities.	» Intensive brand building and customer awareness through traditional above-the-line and below-the-line marketing and promotional campaigns. » Ensuring that our branch operation is profitable by defining payback periods and monitoring branch profitability.	» Strengthened the marketing arm with additional expertise. » Larger spend on marketing, advertising and brand building initiatives. **Effects on Capitals** Increased brand awareness led to enhanced customer perception and relationships – Refer Relationship Capital on page 106 and Intellectual Capital on page 130 for details.

Diagram 3 - Advertising and Promotion Activities Initiated



2015/16
Rs. 85 Mn

Above-the-line

- Target Mass Advertising - Radio/TV
- Press Advertising
- Web Advertising
- Social Media – Facebook

Below-the-line

- Hoardings at Target Town Locations
- Promotions across Branch Network
- Leaflet Printing
- Others

2016/17
Rs. 60 Mn

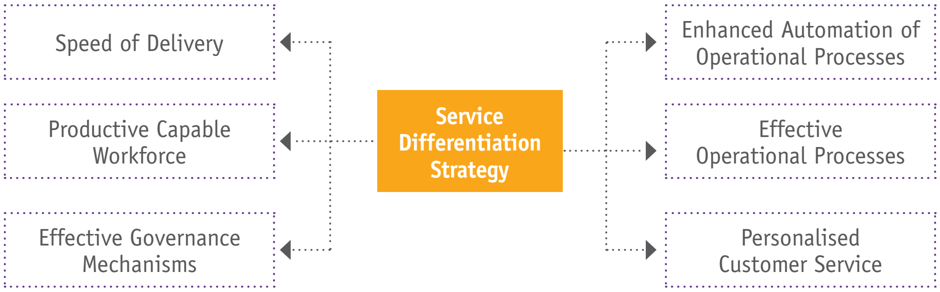
Our Strategy and Resources (Contd.)

Internal and External Business Analysis Outcomes	Strategic Objective	Strategy	Overview of Strategy	Resource Inputs
» Increasing cost of living and other economic factors including rise in interest rates has led to delays and default in borrower repayments. » Increased non-traditional lending bears higher credit risk.	**Short Term Objectives:** » To maintain collection ratio above 90%. » To maintain Non performing lending ratio lower below 4% levels. **Medium to Long Term Objectives:** » Maintaining high standards in asset quality, carrying a NPL ratio that is below 3%.	**Ensuring Asset Quality** **Rationale for Strategy:** Higher yielding assets carry a commensurately higher risk and increases chances of borrower default. Credit recovery needs to be pro-active and timely.	» Monitoring of contracts in arrears supported by aging reports. Dedicated recoveries team and task force to ensure timely follow up action is initiated. » Bringing the expertise of the vehicle valuation, disposal unit and the legal unit to support collections. » Revisiting the existing credit evaluation process and ensuring that the embedded controls are effective and robust by subjecting the process to periodic audits and testing.	Increased investment to station recovery officers at key central points. Enhanced recovery related MIS through ICT support. **Effects on Capitals** Close monitoring of the default risk of borrowers led to prompt collections and effective cash flow management - Refer Financial Capital on pages 81 and 82 for details.
» The need for service quality and improved customer experience to retain/attract customers and remain competitive. » Evolving industry with sophistication and complexity.	**Short Term Objectives:** » Extend a superlative service to customers. » Introduce service standards and inter department service agreements for front ending processes touching customer touch points. » Increase productivity of workforce. **Medium to Long Term Objectives:** » Re-engineer processes running through customer touch points to meet with current customer needs in terms of speed, convenience, digital access as part of ICT strategy. » Carry out benchmark testing against competition and across industry and restructure areas under par.	**Service Differentiation** ***Refer Diagram 4*** **Rationale for Strategy:** Efficient workforce and decentralised management to facilitate faster decision making and speedy approval process to maintain anticipated service standards.	This is a three pronged combined strategy that will sustain service excellence; » Ease of transaction processing and enhance speed of delivery through automation and operational efficiency. » Creating a skilled and knowledgeable workforce. » Governance mechanisms to monitor and implement best practices.	» Large investment earmarked for automation of process. » Investment in digital platforms for customer reach and transaction processing. » Investment in training and development. » Increased investment on risk, compliance, and assurance. **Effects on Capitals** Improved process times and enhanced productivity improved skill inventory and capabilities, driving revenue-Refer Human Capital on pages 121 to 123 and Intellectual Capital on pages 128 to 133 for details.

Management Discussion and Analysis

Our Strategy and Resources (Contd.)

Diagram 4 - Service Differentiation Strategy



Internal and External Business Analysis Outcomes	Strategic Objective	Strategy	Overview of Strategy	Resource Inputs
» Customers prefer the convenience and ease of obtaining all their financial needs under one roof. » In a dynamic industry, differentiation is key to competitive advantage.	**Short Term Objectives:** » Extending after sales service to enhance total product experience. » Forming alliances with insurance companies to obtain competitive insurance policies for MI customers. **Medium to Long Term Objectives:** » Increasing insurance commission income by 20% and workshop revenue by 15% on average per year.	**Ancillary Value Building** **Rationale for Strategy:** To ensure customers enjoy a total one-stop-shop experience, it was necessary that our customers are afforded enhanced product value beyond the core product, offering ancillary services such as insurance, vehicle servicing and repair and also offering deposits services.	» Enhancing capabilities of insurance services staff and vehicle workshop repair and promoting cross selling between loans and deposits product range with special offers.	» Investment to upgrade workshop outlook and restructuring operations. » Resources to promote cross selling avenues. **Effects on Capitals** Enhanced product value and further cemented customer bondings, thus building financial capital through increased revenue-Refer Financial Capital on page 82.
» Corporate practices are closely scrutinised by stakeholders before decisions are made. » Irresponsible corporate actions has a huge impact on reputation in a highly sensitive finance industry.	**Short Term Objectives:** » Making positive impacts on local communities in which we have a presence. » Controlled use of natural resources and environmentally friendly approach to business. **Medium to Long Term Objectives:** » Aspiring for the development of a more sustainable society and environment.	**Corporate Social Responsibility Management** **Rationale for Strategy:** As a corporate upholding a great sense of values and ideologies we believed that our impact to society should not be limited to business dealings and should be further extended.	This involved two aspects: » Expand community interactions and assistance. » Controlled use of natural resources and assist in safeguarding the environment and its habitats.	» Separate annual sustainability budget. » Establishment of a separate high level Committee and support staff who meets regularly. **Effects on Capitals** Social and natural capital development led to indirect push in financial and relationship capital growth-Refer Social Capital on pages 144 to 154 and Natural Capital on pages 134 to 143.

Review of Performance

Strategic Performance Results

The primary strategies we put forth brought us satisfactory results for FY 2016/17, impacting the various forms of capitals deployed, transforming them to meet various stakeholder expectations. These primary strategies coupled with other strategic imperatives generated the desired outcomes and impacts, because of the direct connectivity that prevailed between strategy and the forms of capital deployed. The impact to financial capital from other capital inputs such as relationship capital and intellectual capital was significant due to the correlation identified between the main forms of capital. In particular, the core business strategy adopted continued to deepen our customer interactions, driving total revenue, especially increasing business generated from higher yielding business lines, which helped generate better financial capital. The corporate management monitored the effectiveness of the strategies implemented, comparing actual results periodically against targeted key performance indicators, and took actions to eliminate or minimise gaps noted.

The need to maintain asset quality, to bring down impairment charges and to improve profitability which remained below anticipated levels was a continued area of focus and will be addressed critically during the next financial year.

Capital Wise Performance Summary

Key Strategy	Capital	Key Performance Indicator	Actual 2016/17	Targeted 2016/17	Forecasted for 2017/18
Lending Business : Product Market Strategy	Financial Capital	Total Portfolio Growth (%)	14	> 20	> 12
		Interest Income Growth (%)	23	> 25	> 25
		Net Profit (Rs. Mn)	202	> 500	> 550
	Relationship Capital	Number of Borrowers	50,352	> 55,000	> 60,000
		Number of New Products Launched	2	> 2	> 1
Deposit Business : Market Share Growth Strategy	Financial Capital	Deposit Base Growth (%)	8	15	> 15
		Growth in One Year and Above Deposits (%)	2	15	> 10
	Relationship Capital	Retention Ratio (%)	85	85	> 85
Controlling Margins and Management of Costs	Financial Capital	Cost-to-Income Ratio (%)	67	< 55	< 55
		Net Interest Margin (%)	7.42	> 8	> 8
Marketing Communication Strategy	Relationship Capital	Marketing and Communication Investment (Rs. Mn)	61	> 70	> 80
Asset Quality Management	Financial Capital	Collection Ratio (%)	91	> 90	> 90
		NPL Ratio (%)	6.92	< 4	< 4
	Relationship Capital	Repossessions (Nos)	382	< 300	< 300
		Revival of repossessions (Nos)	58	> 50	> 60
Service Differentiation Strategy	Intellectual Capital	Planned Investment in Automation (Rs. Mn)	274	95	N/A
		New Processes Automated (Nos)	11	10	10
	Human Capital	New jobs created (Nos)	302	150	> 100
		Training Hours per Employee (hours)	44.8	50	60
Provision of a Total Value Added Product	Financial Capital	Cross Selling: Lending against Fixed Deposits (Rs. Mn)	203	> 200	>230
Corporate Responsibility Strategy	Social Capital	Total Community Investment (Rs.)	2,045,511	> 3,000,000	> 4,000,000
		Number of Beneficiaries	4,218	> 5,000	> 5,000
	Natural Capital	Green Investment (Rs.)	149,000	> 500,000	> 600,000
		Employee Volunteerism (Hours)	5,000	> 6,000	> 7,000
		Carbon Footprint (Tonnes of CO_2)	2,447	*N/A	*N/A

**No target as overall was assessed commencing this year.*

Management Discussion and Analysis
Financial Capital Review

"I am content with the performance displayed by Mercantile Investments. I believe the Company has come a long way from its humble beginnings and has achieved steady success overcoming a challenging competitive environment. I would like to wish the Company further success in the years to come."

A. Rajapakse

Mrs. Ainthe Monica Rajapakse
Shareholder - Mercantile Investments and Finance PLC

http://mi.com.lk/value-creation/value-creating-six-capitals/financialcapital/

☑ G4-DMA

Our Approach to Financial Capital Value Creation

In the backdrop of a challenging business environment, we made steady progress during the year in creating financial capital which involved a number of strategic priorities. As primary goals, we achieved sustainable increases in revenue, growth in the loan portfolio and generated steady pre-tax and post-tax profits though being behind expected target levels.

By leveraging on our brand, we were successful in sourcing funding at optimal rates as and when required to maintain required core margins. Expenses were monitored with a renewed focus on cost optimisation initiatives. All of these achievements contributed to overall profitability. However, we could not generate anticipated profitability year-on-year, mainly due to the lowered margins this period from our core business coupled with the impairment charges that was accounted during this period. As witnessed across the industry, core margins continued to diminish on account of the rise in interest rates impacting cost of funding while increases that accrued on yields on loans remained relatively lower. Annual profitability despite being pegged back helped boost retained earnings moderately and with it reasonable investor wealth sustainance.

Key Performance Indicators

	Actual 2016/17	Last year 2015/16	Variance	Targeted 2017/18
Core Revenue Growth (%)	23	5	360%	>20
Net Profit After Tax (NPAT) (Rs. 000)	202,014	505,019	(59.9%)	453,553
Return On Capital Employed (%)	2.57	6.60	(61.1%)	>10
Shareholders' Funds Growth (%)	3	(2)	250%	>10
Cost To Income (%)	67	61	9.8%	55
Non-Performing Impairment Cover (%)	46	88	(47.7%)	>50
Market Share (%)	2.91	2.66	9%	>3
Liquidity Mismatch (Rs. Bn)	5.9	2.66	121.8%	<3

Capital Objectives

» Increase investor wealth

» Capture market share

» Strengthen prudential ratios

» Cost optimisation

» Manage liquidity

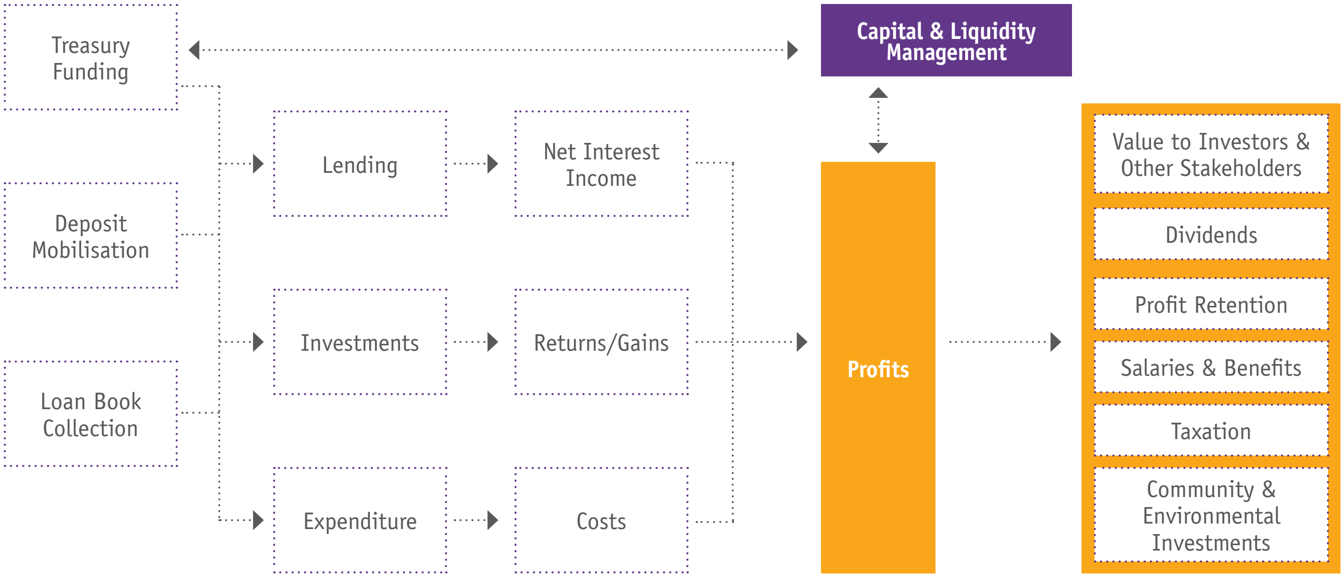
Future Goals

» Ensuring a Return On Capital Employed (ROCE) above 12%

» Increase revenue market share to 4%

» Achieve a zero level maturity mismatch for one year and less assets and liabilities

Financial Capital Value Building Process



Management Discussion and Analysis

Financial Capital Review

Financial Management Strategic Initiatives

- Ensuring adequate liquidity to fund the strategic initiatives and operations of the business
- Sourcing of low cost funding to mitigate the impacts of interest rate risk
- Implementing the recommendations of the Assets and Liability Management Committee on bridging short term maturity mismatches
- Complying with all statutory asset allocation requirements
- Identification of funding options to meet future cash requirements
- Driving a cost conscious culture and cost optimisation initiatives

Financial Management Actions

As a tool of strategic advantage, effective financial management played a critical role in further strengthening MI's financial position and solidity. Initiatives were put in place to ensure that the necessary funding was made available to meet planned loan growth. Liquidity management was handled hand-in-hand with the management of interest rate risks and deemed another high priority area especially considering the dearth in market liquidity at times coupled with the volatile market interest rate movements.

Treasury Management

The treasury department effectively met on-going short term funding needs of the Company and also identified and sourced long term funding that minimised existing assets and liability mismatches, in keeping to the recommendations of ALCO. Sourcing low cost alternatives remained the primary task of the treasury function and accordingly a number of new funding lines were obtained mainly from MI's long standing banking partners. Funding was also sourced through securitisations and commercial paper issuance which increased total borrowing by 26%, in tandem with mobilisation of deposits which continued to remain the main source of funding. (Refer table on Treasury Borrowings Breakdown)

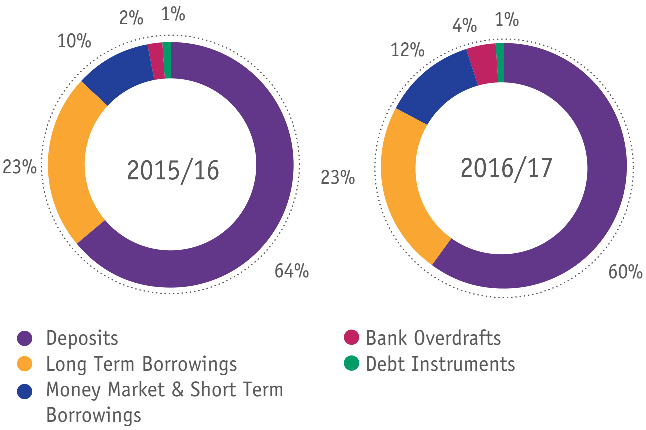
Funding Strategy

With market interest rates moving upward, borrowings remained a cheaper source of funding when compared with deposits for most part of the year. However, we continued to take an aggressive stance in mobilising deposits as well, sourcing shorter tenure fixed deposits and a relatively lower level of longer tenure fixed deposits, to contribute to the funding mix. In addition to deposits, we resorted to sourcing both variable and fixed rate borrowings and focused on sourcing longer term borrowings whilst obtaining medium to short term facilities. This approach enabled the Company to maximise margins and profitability. (Refer graph on Funding Mix)

Treasury Borrowings Breakdown

Source of funding	Total facility value/issue value Rs. Mn	Total facility value/issue value Rs. Mn	New borrowing lines/debt issues	Interest rate range applicable
	FY 2016/'17	FY 2015/'16	FY 2016/'17	FY 2016/'17
Bank Borrowings				
Long Term Loans	5,250	2,191	5	11.5% - 13.25%
Short Term Loans	8,833	9,900	30	9.5% - 14.75%
Money Market Loans	400	600	2	12% - 13%
Commercial Papers				
Commercial Papers	190	Nil	5	12.5% - 13.75%
Others				
Long Term Loans-Securitisations	871	2,000	1	12.7%

Funding Mix



Deposits Mobilisation

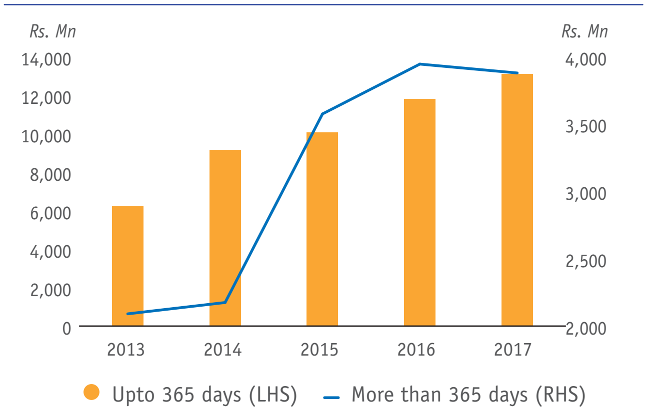
Targeted Deposit Growth 2017/'18	Budgeted Deposit Growth 2016/'17	Actual 2016/'17	Actual 2015/'16	Actual 2014/'15
> 15%	> 15%	8%	15%	20%

The stiff competition prevailing within the sector was further intensified by the indirect competition from the banking sector which afforded comparatively higher returns to depositors than in the past and proved to be challenging. However, by growing the retail fixed deposits by 22%, we endeavoured to maintain a 8% growth in total deposits which rose to Rs. 17,017 Million by the year end. As planned, we continued with our decentralisation programme, making changes to operational procedures including payments and system support, to offer our depositors the required convenience, while affording them attractive returns on par with the industry.

Based on the recommendations of the ALCO, efforts were also directed at mobilising longer tenure deposits to fund higher percentum of lendings which were also of a longer tenure. However, there was more interest shown by depositors to invest in the shorter term deposits, anticipating further rise in interest rates. Despite these sentiments, we successfully mobilised a total of Rs. 816 Million in deposits with tenures exceeding one year which indicated a 2% increase from the year before.

Refer Relationship Capital pages 104 and 105 for deposit product specific information.

Fixed Deposits Maturity



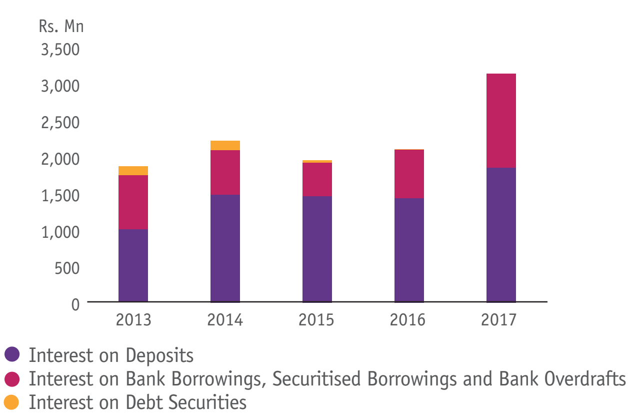
Borrowings

Targeted Borrowings Growth 2017/'18	Budgeted Borrowings Growth 2016/'17	Actual 2016/'17	Actual 2015/'16	Actual 2014/'15
< 10%	< 10%	26%	50%	15%

We resorted to funding part of our lending business through borrowings in line with our strategic goal of reducing the cost of funds to maintain our targeted margins. These borrowings comprised of bank borrowings and securitisations executed during the year. As a result, the total outstanding for borrowings increased to Rs. 11,258 Million, up 26% from a year before. We resorted to money market and other short-term borrowings, overdrafts and debt instruments totalling to Rs. 4,607 Million, and reflecting a rise of 47% year-on-year. In parallel, to reduce the widening gap from short term assets and liability mismatches, we secured long term borrowings, which increased by 15% to Rs. 6,651 Million.

As a result of the funding composition, total interest expenses increased sharply to Rs. 3,136 Million reflective an absolute rise of Rs. 1,038 Million or 49%. Deposits interest cost remained the largest component contributing 59% to total interest expenses with interest cost on borrowings accounting for 41% of total interest expenses.

Analysis of Interest Expenses



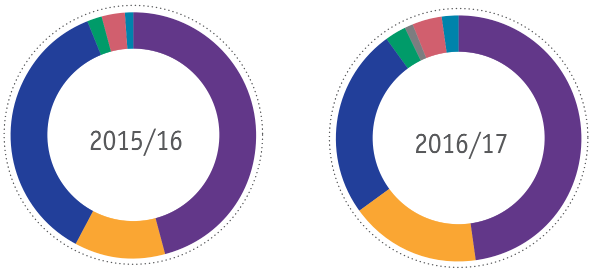
Management Discussion and Analysis

Financial Capital Review

Investment Strategy

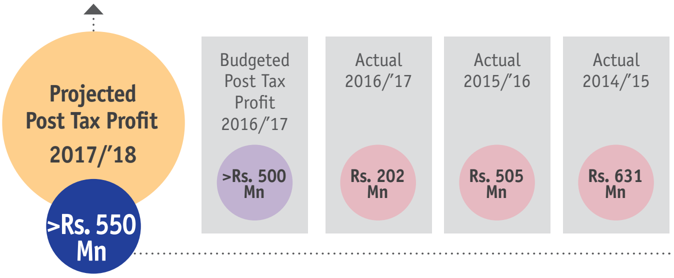
As trading on the stock market continued to be lacklustre due to negative investor sentiments, no investments were made by MI in equity trades this year, but rather, we sold 2.36% of our equity investments and recorded a realised gain of Rs. 60 Million. In order to comply with the CBSL directives on liquidity, we invested in liquid assets transacted through registered primary dealers. We also resorted to money market short term bank placements and deposits primarily to invest excess funds on a temporary basis. An impairment provision was made on account of the government security investments placed in the CBSL appointed primary dealer, details of which is disclosed under notes number 26.1 and 53.4.3 in the financial statements.

Investments in Equity



	2016	2017
● Bank, Finance & Insurance	1,519	1,382
● Diversified Holdings	379	485
● Hotels & Travels	1,181	711
● Investment Trust	1	7
● Manufacturing	55	90
● Power & Energy	4	5
● Land & Property Development	5	2
● Motor	12	19
● Telecommunication	112	118
● Construction & Engineering	17	45
● Trading	7	12

Profitability

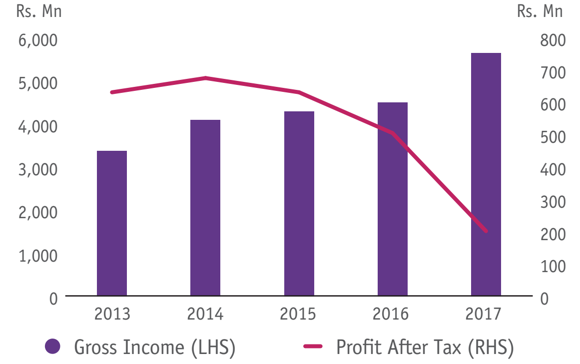


Key Strategic Goals:

- » Creating sufficient investor wealth, by posting robust profitability over Rs. 500 Million
- » Generate an annual profitability growth above minimum growth target of >10%

In the backdrop of a challenging business environment, we managed to record a reasonable profitability for the period under review, but lagged behind planned annual profitability growth expectations. Pre tax and post tax profits for the period under review amounted to Rs. 314 Million and Rs. 202 Million reflecting a decline of 61% and 60% year-on-year respectively. The decrease in profitability levels over the last two years including this year was mainly attributable to the repricing effect impacting core margins coupled with relatively higher impairment charges. In addition, the planned acceleration in total revenue growth was also somewhat pegged back due to continued drawbacks witnessed in the vehicle sales market and controls placed on vehicle financing. However, we generated reasonable profitability; taking advantage of the expanded reach and the strategic focus we had from the inception to expand our capabilities and operating platform, to harness emerging opportunities in the financial markets. In order to boost future profits, we ensured that all new lendings were carried out at optimal yields while a stringent credit review process ensured possible credit risks remain mitigated to keep impairment charges controlled as possible.

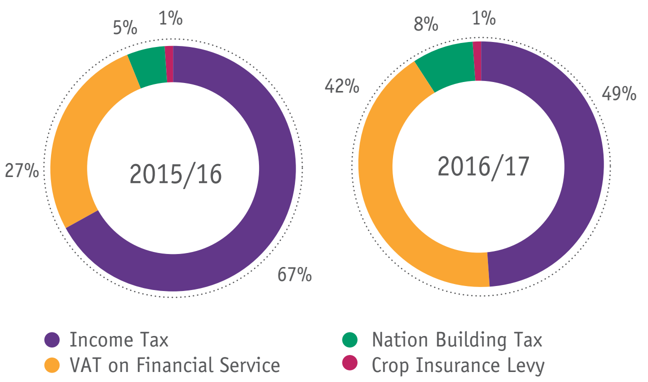
Earnings Performance



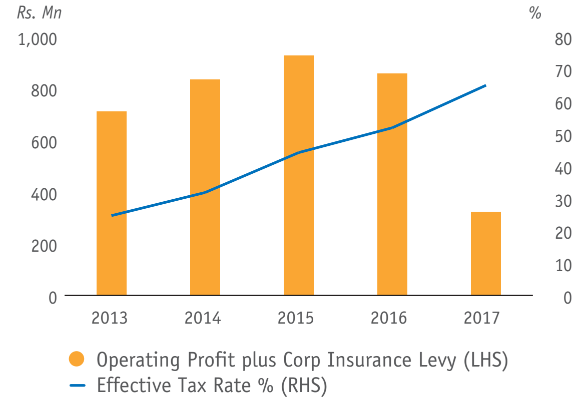
Impact from Taxation

The effective tax rate for the financial sector continued to remain high and was further impacted due to the VAT on financial rate increasing to 15% from 11% starting October 2016. This together with the corporate tax rate of 28% resulted in a high effective tax rate of 64% for MI despite the total corporate tax expense of Rs. 112 Million reflecting a decline of 62% year-on-year, with VAT on financial services also dropping from Rs. 119 Million to Rs. 96 Million. The proposed budgetary changes of 2016 are envisaged to burden the industry further, from the higher tax expenses and the continued high importation tax policy imposed upon the vehicle sales market, resulting in vehicle backed lending opportunities being negatively impacted.

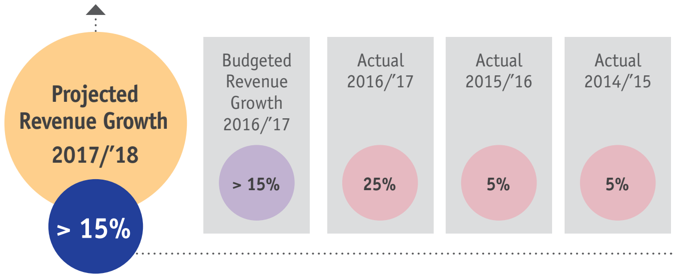
Taxation Breakdown



Operating Profit Vs Effective Tax Rate



Revenue Generation

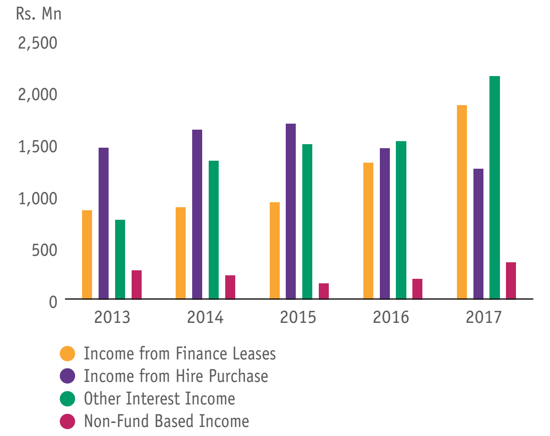


Key Strategic Goals :

- Maintain total revenue growth above 15%
- Increase gross revenue market share by further 1% to 4% by 2020

Total revenue demonstrated a noteworthy rise of 25% peaking at Rs. 5,645 Million, boosted by the satisfactory lending business growth and modest average interest yields. Interest income from the lending business contributed 90% to this year's total revenue while non-fund based income jumped steeply by 81% and remained the other main income source. While clear strategic direction remained on the development of traditional financing business lines and for term lending, based on the changes in the industry dynamics and customer preferences, attention was also paid to earning new revenue streams. The introduction of new lending products and innovative tailor made credit solutions, contributed significantly in growing revenue, by leveraging on the investment in branch expansion.

Composition of Gross Income



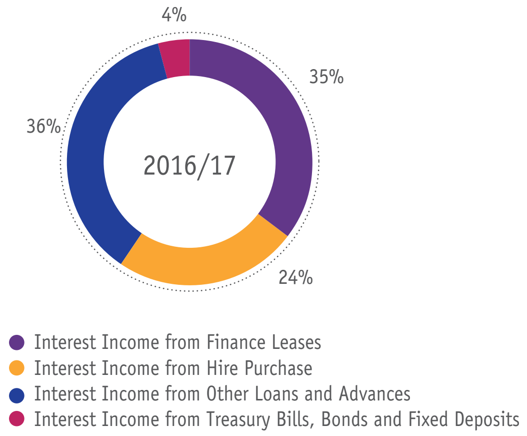
Management Discussion and Analysis

Financial Capital Review

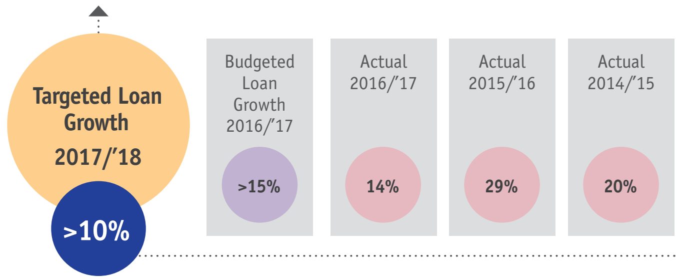
Total Interest Income

Despite the industry's very competitive and challenging business conditions, total interest income rose moderately to Rs. 5,286 Million, up by 23% from previous year, propelled primarily by the growth in the lending business. Other loans and advances remained the key interest income generating product for MI mainly driven by vehicle loans, microfinance and property backed lending, with a 36% contribution, while interest income from hire purchase financing continued to dip after the exclusion of value added tax on leases since 2015. In contrast, leases performed well contributing 35% to interest income. Nevertheless, interest income from investing in government securities and banks mainly for liquidity purposes stood at 4%, but generated comparatively lower returns.

Components of Interest Income



Lending Portfolio and Disbursements



Key Strategic Goals :

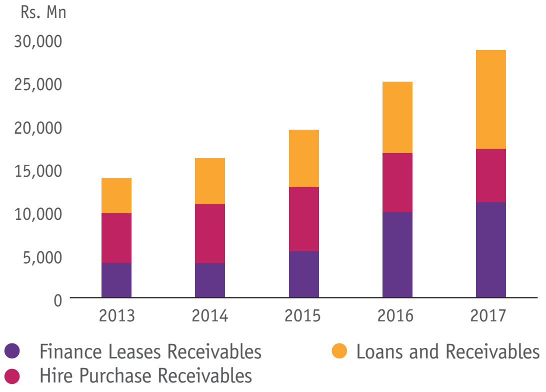
» Maintaining a steady lending portfolio growth of 15%

» Striving for an average yield above minimum threshold to keep core margins above 8%

Despite the prevailing sluggish market conditions of the vehicles sales market, which was further impacted by the high importation costs on new vehicle imports and restrictions imposed on related credit growth, particularly the controls placed through a maximum loan to value ratio, we maintained steady portfolio growth momentum throughout the year, on par with the industry. As a result of the focused strategic initiatives implemented, total lease outstanding rose commendably to Rs. 11,094 Million, reflecting an increase of Rs. 1,168 Million or 12% growth year-on-year. Similarly, total loan portfolio topped Rs. 28,646 Million, up by 14% year-on-year. Other loans and advances generated the highest revenue for the Company as a single product and continued to be popular among most customer segments. Other loans and advances grew impressively by 37% year-on-year to Rs. 11,367 Million.

With the import of brand new vehicles slowing down due to escalating taxes, duties and levies, we witnessed the demand for purchase of second hand vehicles increasing. It was also very evident that the ongoing economic resurgence and increasing construction activity propelled the need for financing, particularly to acquire property, machinery and construction related vehicles. This together with other emerging opportunities resulted in new avenues for revenue generation. (Refer relationship capital pages 98 to 103 for more details)

Composition of Total Lending



Portfolio Quality

Targeted NPL Ratio 2017/'18

< 4%

Budgeted NPL Ratio 2016/'17	Actual 2016/'17	Actual 2015/'16	Actual 2014/'15
< 3%	**6.92%**	**3.39%**	**4.19%**

** Non-performing lending ratios have been computed based on CBSL time based provisioning regulations.*

Key Strategic Goals :

» Implementing an effective credit risk review mechanism

» Strong recovery drive to speed up collections and to keep collections above 95%

» Recovery actions to bring down non-performing loan balances

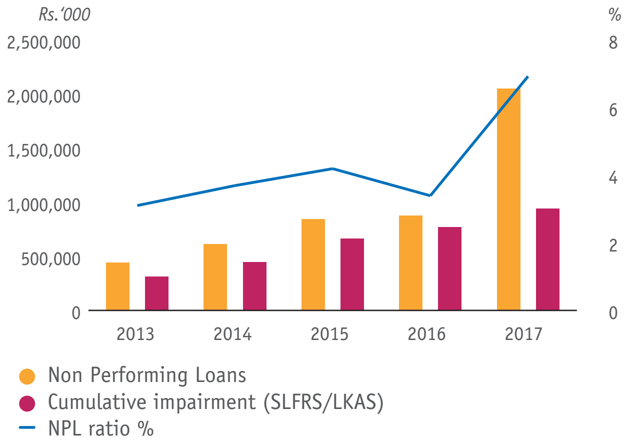
» Strengthening the credit evaluation process and required documentation

All credit was subject to a formal credit evaluation process, and this involved obtaining of security, guarantors and other requisites and more stringent credit requirements being applied for higher risk disbursements, to eliminate possible credit losses. Post disbursement, stringent recovery actions were initiated to prevent certain contracts moving into arrears, leading to prompt regularisation which controlled undue increases in non-performing lending levels. Nevertheless, as a consequence of changes in business conditions few large facilities though adequately backed by security, moved into the non-performing category. This resulted in the NPL ratio steeply moving upward to 6.92%.

As a recovery policy in easing collections, immediate attention was given to the first six months of a contract and contracts in arrears between three to six months. This prompt monitoring process kept overall collections satisfactory at 91%, but below the internal threshold of 95%. Conversely, to manage problematic default accounts we resorted to tougher recovery measures that included repossession of assets, mostly vehicles and resorting to legal recourse. A specialised recovery team called the Special Recoveries Force (SRF) was put to action to provide a 24/7 recovery effort. Additional SRF teams were deployed to speed up actions and this contributed to these satisfactory collection levels.

MI's specialised internal valuation and disposal unit played an important role, coordinating with the recovery division to dispose ceased vehicles promptly. In parallel, our strong legal unit provided the required legal support and advice to the recovery division and was instrumental in initiating timely action against highly problematic defaulters, and also in expediting cases expeditiously.

Total Non Performing Loan Status and Impairment



Actions on Problematic Borrowers

Product	Cases filed in 2016/17	Cases filed in 2015/16	Successfully completed cases in 2016/17
Hire Purchase	36	169	80
Finance Leases	39	118	45
Personal Loans	04	08	04
Property Mortgage Loans	05	20	01
Vehicle Loans	06	22	14

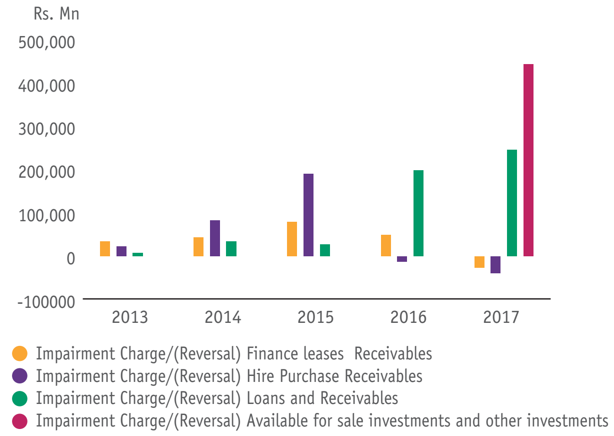
Management Discussion and Analysis

Financial Capital Review

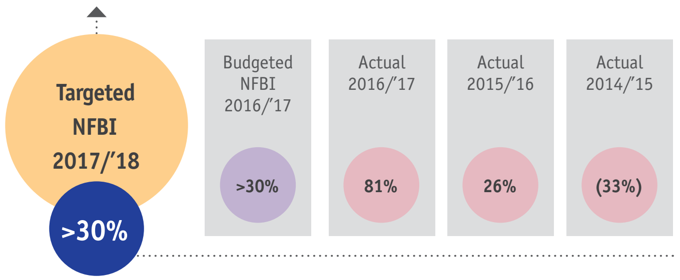
Accounting for Impairment Charges

The impact of lending book impairment charge/(reversal) to Statement of Comprehensive Income was computed assessing the individual and collective impairment charge/(reversals) in compliance with LKAS/ SLFRS requirements. In keeping with LKAS/SLFRS impairment requirements, all necessary provisions were made on account of identified "bad credit accounts". Total impairment charges increased by 166% remaining significant at Rs. 625million, mainly on account of impairment arising from loans and advances category and other. The cumulative impairment provision remained moderate against the non-performing loans, with the provisioning cover dropping to 46% from 88% observed in the previous year.

Analysis of Impairment Charge/(Gain)



Other Income/Non-Fund Based Income (NFBI)

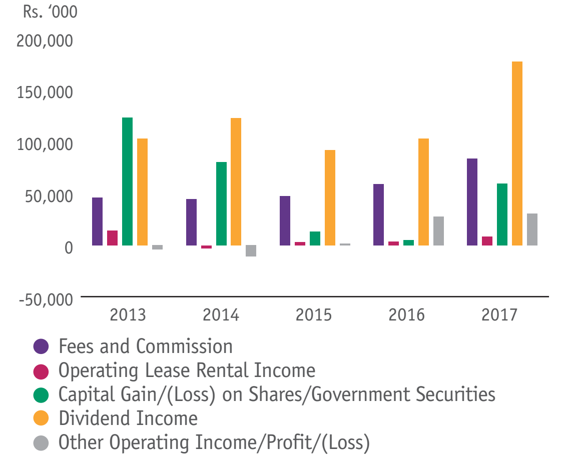


Key Strategic Goals :

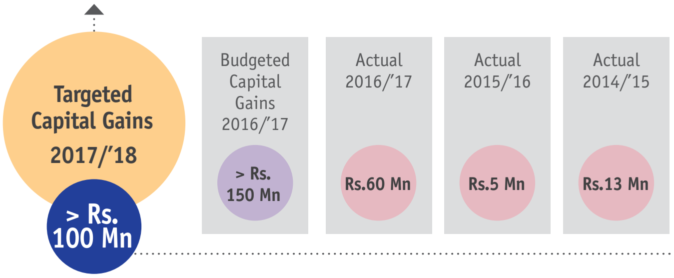
- Increasing contribution from non-fund based revenue, by maintaining steady annual NFBI growth
- Maximise returns from trading in equity portfolio

Based on the strategic measures undertaken and the optimistic predictions, other income/NFBI to total revenue remained higher in absolute terms increasing from Rs. 198 Million to Rs. 359 Million, up significantly by 81% year-on-year. The main reasons being the higher income derived from dividends and trading in equity portfolio. In addition, both the insurance support division and workshop service and repair divisions performed quite satisfactorily with related income up 42% and 12% respectively in tandem with increased transaction levels.

Non-Fund Based Income



Equity Portfolio Returns



Declaration of satisfactory dividend payouts by both the banking and leisure sectors boosted total dividend income which amounted to Rs. 177 Million, up by 72% year-on-year and remained the largest NFBI constituent. Realised capital gains on equity too was up staggeringly by 1,058% amounting to Rs. 60 Million but remained lower than planned due to most share prices declining in tandem with the market indices.

The sector-wise composition of MI's share portfolio did not indicate any major shift between sectors from last year. A major 79% comprised of investments in hotels, banking and finance and insurance sectors.

(Refer pages 316 to 318 in the Financial Statements Note on equity portfolio and pages 356 and 357 in the Financial Statements Risk Note)

Net Interest Income (NII) and Margins

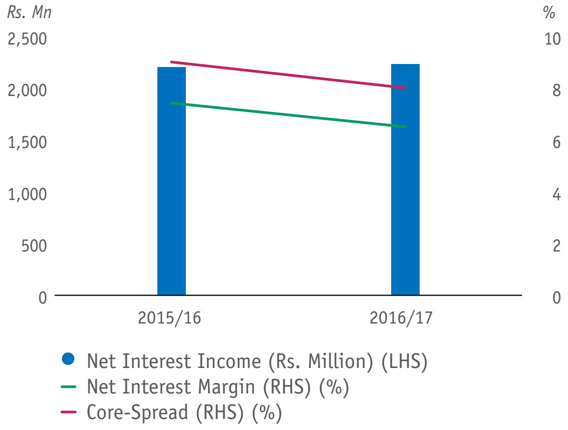
Key Strategic Goals:

» Recording a minimum growth of 15% in NII

» Maintaining average Net Interest Margin (NIM) above 9% and core spread to be above 8%

Total NII contracted to Rs. 2,150 Million, reflecting a moderate decline of 2%, and was below anticipated levels. The slowdown in NII was mainly due to the increased cost of funding. The re-pricing effect caused cost of funding to rise and core margins to be squeezed, resulting in Net Interest Margins (NIMs) and core spread being pegged back. As a counter strategy of improving NIMs, higher yielding term based lending was promoted more aggressively than before and strictly complied with the policy to refrain from doing business below break-even levels as done in the past.

Net Interest Income, Net Interest Margin and Spread



Management Discussion and Analysis

Financial Capital Review

Operating Expenses

Key Strategic Goals :

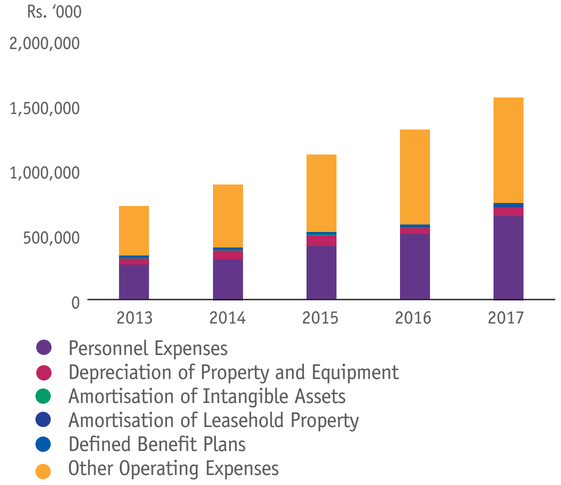
» Cost optimisation in the wake of expanding operations and inflationary factors

» Maintaining the cost to income ratio below 55%

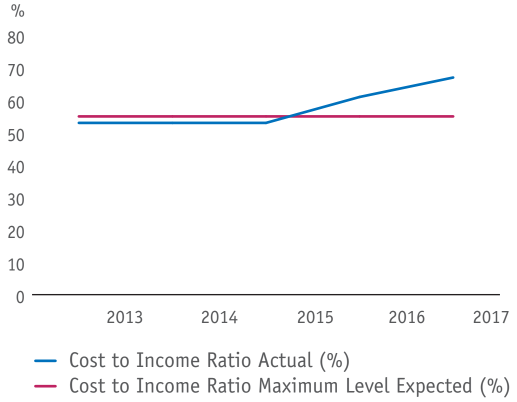
Increased utilisation of resources that include greater manpower requirements coupled with general inflationary effects on goods and services caused total operating expenses of the Company to move upward to Rs. 1,562 Million, reflecting an increase of 19% year-on-year. Personnel costs remained the largest overhead cost component, increasing 28% to Rs. 650 Million because of the combined effect from new recruitments being made in the wake of branch expansions and the annual salary revisions effected. Business expansion also led to the escalation of other operating expenses (excluding personnel cost) which increased by 13% to Rs. 912 Million.

The cost to income ratio moved up to reach 67% and was above minimum expected threshold. The lag in revenue generation of branches established in the last couple of years and the costs incurred on branches opened in 2017 kept the ratio above minimum threshold limits. However, we expect the ratio to gradually improve once these branches start generating revenue at full capacity.

Composition of Operating Expenses



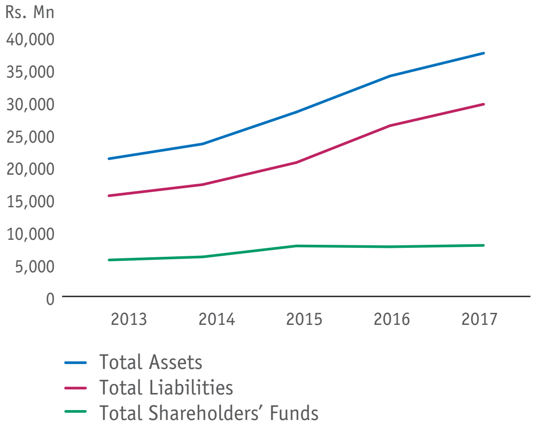
Cost to Income Ratio



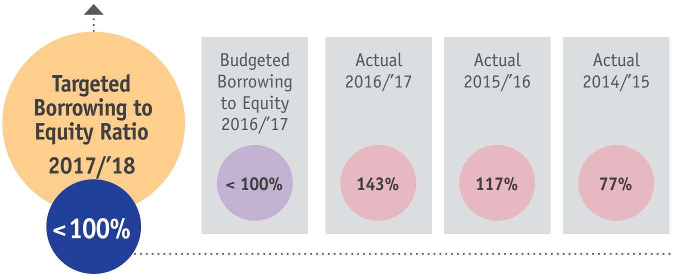
Total Assets, Total Liabilities and Shareholders' Equity Movement

Growth in the lending business propelled total assets to advance to Rs. 37,493 Million, an increase of Rs. 3,528 Million in absolute terms and 10% increase. Loans and advances receivable remained the largest asset component accounting 76% of total assets. Total liabilities increased by 13%, advancing to Rs. 29,625 Million, driven by the high borrowings and aggressive deposit mobilisation. However, shareholders' funds increased marginally by 3% and were reported at Rs. 7,867 Million by the balance sheet date. The moderate post tax profits recorded for this period together with an insignificant movement in the fair value of equity investments held under the available-for-sale financial assets, pegged back expected growth in the shareholders' funds. We remain optimistic on maintaining sustainable equity capital growth in the next few years, based on our planned growth strategies and investments already made in increasing our reach.

Total Assets, Liabilities and Shareholders' Funds



Gearing Management



Key Strategic Goal :

- » Maintaining a debt to equity percentum that reflects ideal funding blend, fortifying continued financial solidity

The gearing ratio for the second year stood above the maximum threshold, as management continued to resort to higher borrowings in comparison to a decelerating growth recorded in total equity on account of moderate retained profits and no movement in stated capital. Despite deposit growth slowing down initially, as the year neared closure, we endeavoured to reduce our borrowings and focused on aggressive deposit mobilisation, restraining the ratio from increasing further.

Management Discussion and Analysis

Financial Capital Review

Cash Flow Management

Key Strategic Goal:

» Maintaining adequate liquidity to meet daily cash needs, ad hoc requirements and future long term funding requirements

» Managing interest rate risks

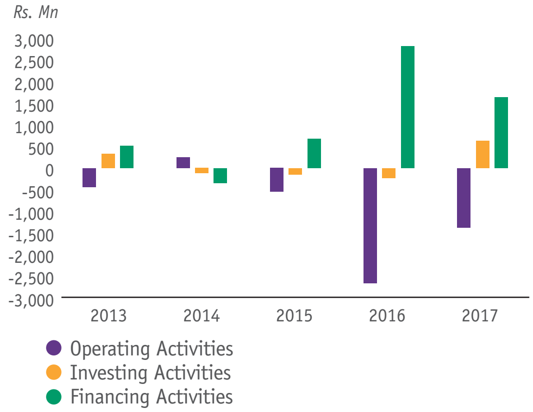
Cash Flow Position

MI's cash and cash equivalents as at the reporting date increased from a year before by Rs. 900 Million to Rs. 1,245 Million due to cash flow movements arising from our operating activities together with financing and investing activities carried out for the period.

Cash Flow from Operating Activities

Net movement of MI's operating cash flows shifted from a negative of Rs. 2,658 Million a year before, to a negative of Rs. 1,375 Million as at the reporting date. The inflow of cash from operating activities arose mainly from interest and commission receipts and through the efficient management of operating activities. However, negative operating cash outflow resulted mainly due to funds advanced to customers, interest payments, personnel costs and other overheads.

Cash Flow Analysis



Cash flow from Investing Activities

MI's cash flow from investing activities reflected an inflow for the period under review amounting to Rs. 636 Million, compared to an outflow of Rs. 228 Million recorded last year. Sale of non-dealing securities together with the sale of property, plant and equipment, resulted in the net inflow.

Cash Flow from Financing Activities

Cash flow from financing activities showed a cash inflow totalling Rs. 1,639 Million as at 31st March 2017, compared to a positive cash flow of Rs. 2,823 Million recorded during the previous period. The decrease in cash inflow was attributable to the higher level of debt servicing undertaken during this period.

Refer liquidity risk management on pages 254 to 257 of the Risk Report for further insight to cash management.

☑ G4-FS 6

Divisional Business Performance

Branch/Service Centre Performance

Apart from sustained Western Province business, branches beyond also grew their lending book satisfactorily by 17%, contributing 30% to total lending interest income. Moreover, the deposit mobilisation from branches was steadily on the rise, contributing 13% to the traditional Head Office deposit canvassing process, which reflected a commendable growth of 85% year-on-year for branch deposit mobilisation. (Refer table on Geographic Dispersion of Segment Revenue given below)

Branch/Service Centre wise Financial information - Visit MI website

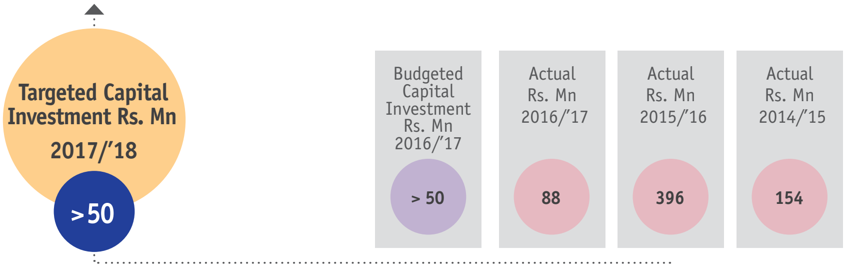
http://mi.com.lk/value-creation/value-creating-six-capitals/financialcapital/

Segmental Performance

Lease, Hire Purchase and Loan and Advances Segments

From the core business of lending, Finance Lease segment was the highest revenue generating segment recording a Rs. 1,874 Million in revenue, up 42% over last year. There was a marked drop in the hire purchase segment with lowered demand, with greater management interest shown to boost loan and advances revenue segment which grew by 38%.

Other Capital Performance Perspectives



Further description of the material and distinctly identifiable segments are explained in the Financial Statements under the business segments note on pages 346 and 347.

Capital Investment Outlay

Having accumulated a strong capital base, there was adequate liquidity to proceed with making the required capital investments, to support our planned strategy and operational requirements. In particular, out of the capital investments earmarked, a relatively higher percentage will be allocated to upgrade the existing ICT systems, to improve ICT capabilities and performance standards for the future.

Capital Investments incurred/to be incurred - Visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/financialcapital/

Capital investments incurred/to be incurred

Regulatory Capital Adequacy Position

MI's policy on capital is to maintain a strong capital base through growth and reinvestment to ensure investor, creditor and market confidence is maintained with trust being at the core of our brand promise, while taking a long term view in creating value that is sustainable for all our stakeholders. MI is known for prudential financial management capabilities. MI's core capital adequacy ratio and total risk weighted capital adequacy ratio stood well above the regulatory requirements again this financial year, reflecting its financial strength and ability to withstand various shocks from the external environment.

Tire 1 core capital as at 31st March 2017 amounted to Rs. 6,181 Million, leading to a strong core capital ratio of 17.17% (minimum ratio 5%) while similarly the total risk-weighted capital ratio stood at 14.26% above the regulatory minimum of 10%.

A detailed analysis of MI's Capital Adequacy position is given under the Financial Risk Management pages 358 to 360.

Geographic Dispersion of Segment Revenue (Rs. 000)

	Lease	Hire Purchase	Loans and Advances	Investments	Workshop and service station	Other	Total
Central Province	3,835	268	857	-	-	-	4,960
Eastern Province	101,488	22,387	9,284	-	-	-	133,160
North Central Province	143,136	46,003	57,927	-	-	-	247,066
North western Province	121,949	74,484	74,469	-	-	-	270,902
Sabaragamuwa Province	148,248	47,440	141,979	-	-	-	337,667
Southern Province	219,174	118,487	265,072	-	-	-	602,734
Western Province	1,136,160	953,291	1,369,731	236,546	90,434	262,881	4,049,043
Total	1,873,991	1,262,361	1,919,319	236,546	90,434	262,881	5,645,532

Management Discussion and Analysis

Financial Capital Review

Wider Economic Impact

Management Approach

In being a responsible and committed corporate citizen, we endeavour to align our corporate strategy with national priorities, while embedding global best practices in managing our triple bottom line, which comprises of the economic, environmental and social impacts of the business. We also remain true to our core values and adhere to the highest ethical standards, in keeping with our overarching strategy that focuses on a triple bottom line approach. Our aim is to differentiate ourselves as an exceptional financial service provider, while ensuring sustainable value creation for our stakeholders and contributing eventually to both the LFC sector and our national economy. (Refer Diagram on Wider Economic Impact given below)

☑ *G4-EC 7*

Contribution to the Economy

Our economic impact is far reaching, as we cater to a wide cross section of individuals and corporates alike across various regions and communities. MI's value addition to the economy in recent years has witnessed an annual increase year-on-year, as evident from the financial results, which has resulted in the accumulation of shareholder wealth, employee benefits and contribution to the Government by way of taxes increasing annually.

We are very receptive towards the changing financial needs of the public, and tailor our lending facilities to suit both individuals as well as corporates alike to fund their financial requirements that ultimately result in economic prosperity of the individuals and economic value addition for the corporate entities which culminate in positive contributions that increase per capita income levels and the gross domestic product at a national level.

Our reach extends to communities even in the remotest areas of the country, and our financial solutions made easily accessible to all have evolved from traditional financing to other forms of credit, such as micro based funding and personal lending. The success achieved by the Company in its fifty plus years of corporate existence has always been shared with our key stakeholders, with a cascading effect across society resulting in economic prosperity in the communities in which we operate, and to the industry and country at large. Furthermore, having identified the role of small businesses as a powerful wheel driving the economy of local communities and a critical catalyst in driving prosperity in the national economy, MI is committed to extending our support to this sector by offering a specialised product range and the exceptional service quality extended through our branch network.

Direct Economic Impact

☑ *G4-EC 1*

Direct Economic Value Generated and Distributed

During the year, the Company though being behind anticipated pofitability targets was able to record satisfactory profitability levels reaffirming its commitment towards continuous wealth creation for its investors amidst of a volatile and competitive business environment. With the expansion of our islandwide footprint and innovative financial solutions, MI has extended its reach beyond the Western Province. In extending our reach in 2017, we now contribute to the economic and social development of Veyangoda, Thambuththegama, Gampola, Wattala and Avissawella towns through our value offering and business presence.

In terms of value to the economy, MI's total value addition rose from Rs. 4,592 Million to Rs. 5,750 Million for the financial year ending 31st March 2017 up 25%. Keeping long term growth prospects of the Company in mind, 5% of this year's total value addition was retained within the business and the remainder was distributed. A distribution of 12% was distributed as emoluments and statutory dues to employees and 4% by way of taxes to the Government.

Wider Economic Impact

Direct Economic Impacts

Increase in direct economic value generated Rs. 1,158 Mn
Contribution as Tax Rs. 224 Mn
Market Capitalisation Rs. 7,756 Mn

Employment Creation

Number of New Jobs 302
Total Employee Benefits Rs. 678 Mn

Indirect Economic Impacts

Total Disbursement Rs. 20,105 Mn
Funds Mobilisation Rs. 17,017 Mn
Number of Customer Partnership 39,742

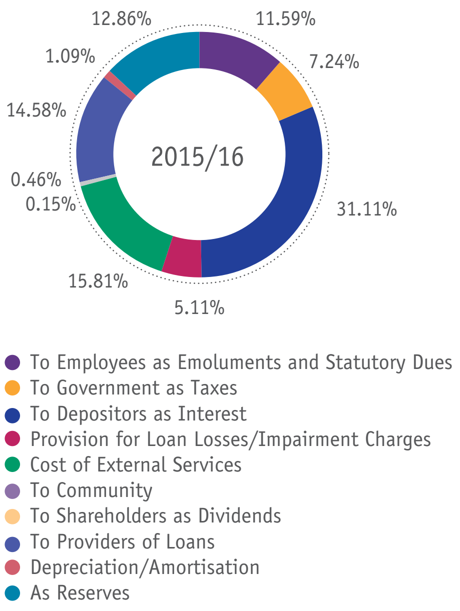
Community and Environmental Investments

Community & Environmental Investment Rs. 2 Mn
Number of Individuals Socially Supported 4,214

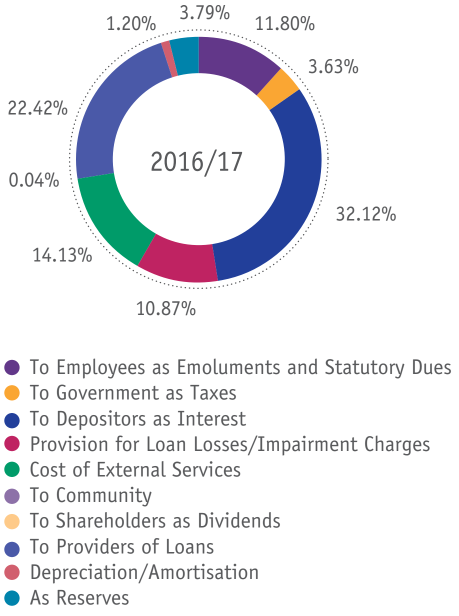
Direct Economic Value Generated and Distributed (Rs. 000)

For the Year ended March 31st	2017		2016		2015		2014		2013	
Direct Economic Value Generated										
Interest Income	5,286,059		4,301,828		4,129,395		3,861,558		3,087,726	
Commission Income	83,622		58,927		47,554		44,402		45,937	
Investment Income	59,542		5,143		13,049		80,512		123,179	
Share of Associate Company Profit	104,194		91,675		113,795		105,798		95,459	
Others	216,309		134,377		96,290		109,338		113,245	
	5,749,726		4,591,950		4,400,083		4,201,608		3,465,546	
Economic Value Distributed										
To Employees as emoluments and statutory dues	678,232	12%	532,029	12%	437,628	10%	335,849	8%	291,804	8%
To Government as Taxes	208,735	4%	332,306	7%	313,592	7%	279,760	7%	236,173	7%
Operating Costs										
To Depositors as Interest	1,847,009	32%	1,428,676	31%	1,456,321	33%	1,477,307	35%	1,001,092	29%
Provision for Loan Losses/Impairment Charges	625,066	11%	234,816	5%	295,741	7%	160,445	4%	64,318	2%
Cost of External Services	812,462	14%	725,945	16%	597,162	14%	482,085	11%	382,973	11%
To Community	2,045	0%	7,053	0%	3,063	0%	2,339	0%	1,820	0%
Payments to Providers of Capital										
To Shareholders as Dividends	-	0%	21,042	0%	88,677	2%	30,060	1%	82,665	2%
To Providers of Loans	1,289,209	22%	669,702	15%	491,462	11%	738,176	18%	866,608	25%
Economic Value Retained within the Business										
- as Depreciation/Amortisation	69,186	1%	49,994	1%	86,896	2%	71,174	2%	50,876	1%
- as Reserves	217,782	4%	590,387	13%	629,541	14%	624,413	15%	487,217	14%
	5,749,726	100%	4,591,950	100%	4,400,083	100%	4,201,608	100%	3,465,546	100%

Economic Value Distributed



Economic Value Distributed



Management Discussion and Analysis

Financial Capital Review

Increasing Tax Contributions

We continue to contribute to the national exchequer by way of annual taxes, but observed a 37% decrease this period. Having contributed over Rs. 200 Million, we understand that MI's tax contribution is a source of indirect support to the ongoing infrastructure development and social upliftment initiated by the State.

Refer Financial Capital Page 79, describing tax components.

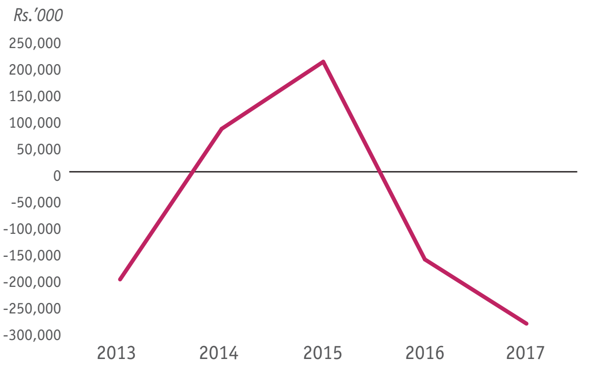
Economic Value Added

MI's level of contribution to the national economy has grown over the last five decades, although moderate earnings resulted in a negative Economic Value Addition (EVA) of Rs. 285 Million being reported. Steep increase in risk free investments widened the negative gap and the challenging condition made it difficult in achieving the much higher anticipated EVA.

Economic Value Added (Rs. 000)

As at 31st March	2017	2016	2015	2014	2013
Invested Equity					
Shareholders' Funds	7,867,265	7,654,232	7,779,765	6,266,385	5,706,358
Add: Provision for Impairment	1,381,633	770,887	660,743	447,782	311,530
Total	9,248,898	8,425,119	8,440,508	6,714,167	6,017,888
Earnings					
Net Profit After Tax	202,014	505,019	631,272	675,362	630,791
Add: Impairment Charges for Loans and Advances	625,066	234,816	295,741	160,445	96,358
Less: Bad Debt Written Off	(14,320)	(124,672)	(82,780)	(24,193)	(32,040)
Total	812,760	615,163	844,233	811,614	695,109
Cost of Equity (based on 12 months Weighted Average Treasury Bill Rate plus 2% for the Risk Premium)	12.43%	9.25%	8.41%	11.48%	15.25%
Cost of Average Equity	1,098,440	780,035	637,254	730,820	897,596
Economic Value Added	(285,680)	(164,872)	206,979	80,794	(202,487)

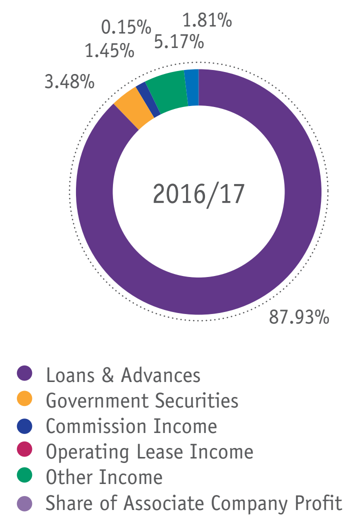
Economic Value Added



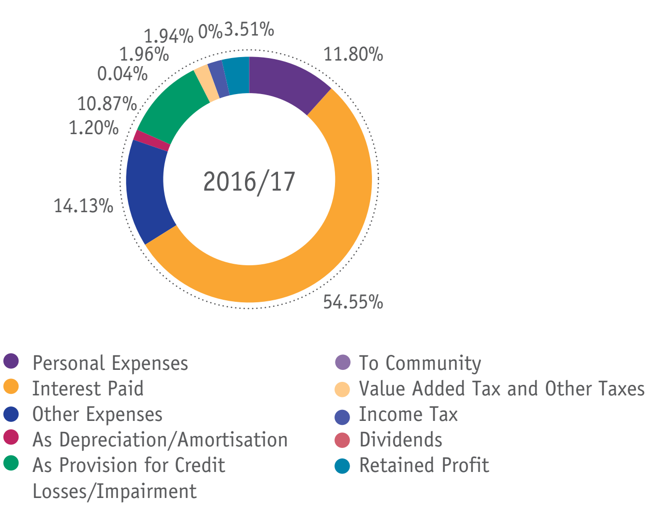
Sources & Utilisation of Income (Rs. 000)

For the Year ended March 31st	2017		2016		2015		2014		2013	
Sources of Income										
Loans & Advances	5,055,670	87.93%	4,172,079	90.86%	3,999,741	90.90%	3,731,971	88.82%	2,994,935	86.42%
Government Securities	200,207	3.48%	98,809	2.15%	92,161	2.09%	81,946	1.95%	59,584	1.72%
Commission Income	83,622	1.45%	58,927	1.28%	47,554	1.08%	44,402	1.06%	45,936	1.33%
Operating Lease Income	8,507	0.15%	3,785	0.08%	2,926	0.07%	(2,738)	(0.07%)	14,270	0.41%
Other Income	297,526	5.17%	166,675	3.63%	143,906	3.27%	240,229	5.72%	255,360	7.37%
Share of Associate Company Profit	104,194	1.81%	91,675	2.00%	113,795	2.59%	105,798	2.52%	95,459	2.75%
Total	5,749,726	100.00%	4,591,950	100.00%	4,400,083	100.00%	4,201,608	100.00%	3,465,544	100.00%
Utilisation of Income										
To Employees										
Personal Expenses	678,232	11.80%	532,029	11.59%	437,628	9.95%	335,849	7.99%	291,804	8.42%
To Suppliers										
Interest Paid	3,136,218	54.55%	2,098,378	45.70%	1,947,783	44.27%	2,215,483	52.73%	1,867,700	53.89%
Other Expenses	812,461	14.13%	725,944	15.81%	597,161	13.57%	482,085	11.47%	382,973	11.05%
As Depreciation/Amortisation	69,186	1.20%	49,994	1.09%	86,896	1.97%	71,174	1.69%	50,876	1.47%
As Provision for Credit Losses/Impairment	625,066	10.87%	234,816	5.11%	295,741	6.72%	160,445	3.82%	64,318	1.86%
To Community	2,045	0.04%	7,053	0.15%	3,063	0.07%	2,339	0.06%	1,820	0.05%
To Government										
Value Added Tax and Other Taxes	112,838	1.96%	141,090	3.07%	119,926	2.73%	109,902	2.62%	73,985	2.13%
Income Tax	111,664	1.94%	297,626	6.48%	193,666	4.40%	169,858	4.04%	162,188	4.68%
To Shareholders										
Dividends	-	0.00%	21,042	0.46%	88,677	2.02%	30,060	0.72%	82,665	2.39%
To Reserves										
Retained Profit	202,015	3.51%	483,978	10.54%	629,541	14.31%	624,413	14.86%	487,217	14.06%
Total	5,749,726	100.00%	4,591,950	100.00%	4,400,083	100%	4,201,608	100%	3,465,546	100%

Sources of Income



Utilisation of Income



Management Discussion and Analysis

Financial Capital Review

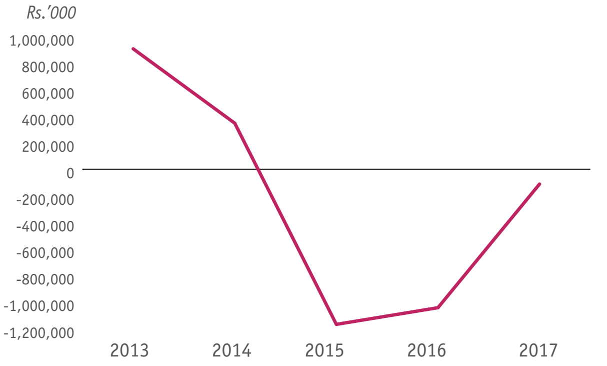
Market Value Addition

MI obtained listing status under the Diri-Savi Board of the Colombo Stock Exchange in June 2012, the ordinary shares of the Company traded only twice to date since then, but the last traded share price rose to Rs. 2,580 per share as at 31st March 2017. Despite the increase, MVA remained negative but continued to improve. The Company expects the MVA to improve once greater trading takes place in future.

Market Value Added (Rs. 000)

As at 31 March	2017	2016	2015	2014	2013
Market capitalisation/ Market value of equity	7,756,382	6,613,200	6,613,200	6,613,200	6,613,200
Less: Equity owner's funds					
Shareholders' funds	7,867,265	7,654,232	7,779,765	6,266,385	5,706,358
Total equity owners' funds	7,867,265	7,654,232	7,779,765	6,266,385	5,706,358
Market value added	(110,883)	(1,041,032)	(1,166,565)	346,815	906,842

Market Value Added



Indirect Economic Impact

☑ *G4-EC 7*

Subscribing to the Finance Industry Growth and Stability

As a responsible corporate citizen we have committed to build trust and confidence with both the regulators and the general public through our compliance with statutory regulations, the establishing of robust risk and governance frameworks, and effective risk management and ethical business practices which ultimately contribute to the growth and stability of the finance sector.

MI's Credit Support to Various Sectors

Industry/sector credit has been extended	Total disbursements by industry/sector		Number of customers in industry/sector enjoying credit		% Growth	
	2016/17 Rs. 000	2015/16 Rs. 000	2016/17	2015/16	Disbursement	Customers
Agriculture	546,205	655,371	1,579	2,078	(16.66)	(24.01)
Commercial	4,447,950	4,504,932	23,677	11,545	(1.26)	105.08
Consumption	731,975	641,107	4,240	1,134	14.17	273.90
Finance	132,980	153,138	67	75	(13.16)	(10.67)
Housing & Property	464,312	674,484	162	119	(31.16)	36.13
Industrial	515,631	645,687	417	921	(20.14)	(54.72)
Services	9,676,463	9,411,818	6,303	6,798	2.81	(7.28)
Tourism	376,534	250,370	157	138	50.39	13.77
Lending for Infrastructure Development Projects	-	15,500	-	2	(100.00)	(100.00)
Others	3,213,342	2,607,108	3,140	2,416	23.25	29.97

☑ G4-EC 8

Significant Indirect Economic Impacts, Including The Extent of Impact

Province credit has been extended	2016/17			2015/16			Change in total disbursment Rs. 000
	Total disbursements by province in FY 2016/17 Rs. 000	Number of customers in province enjoying credit as at 31st March 2017	Number of Branches	Total disbursements by province in FY 2015/16 Rs. 000	Number of customers in province enjoying credit as at 31st March 2016	Number of Branches	
Central	284,759	214	1	226,947	142	-	57,812
Eastern	395,658	566	2	456,534	633	2	(60,876)
North Central	838,329	4,730	3	754,816	781	2	83,512
North Western	1,527,854	6,158	3	1,264,559	2,550	3	263,295
Northern	11,415	12	-	9,242	12	-	2,173
Sabaragamuwa	1,306,760	5,710	4	1,133,099	4,637	4	173,661
Southern	2,013,265	4,692	5	2,060,060	4,195	5	(46,795)
Uva	139,612	442	-	169,955	721	-	(30,343)
Western	13,587,741	17,218	18	13,484,304	11,555	15	103,437

Employment Creation

We have created significant job opportunities by expanding our workforce exponentially in keeping with business growth. We have invested in uplifting their skills and the working environment which enabled us to be recognised as one of the top fifteen “Best Companies to Work For”. We have distributed 12% of our earnings as emoluments and statutory dues. The employment opportunities generated over the last five years, the employee hiring growth percentage and the total employment outreach is given on page 121 of the Human Capital Report.

☑ G4-EC 1

Community & Environmental Investment

We are profoundly aware of the importance of embedding corporate responsibility into our business decisions. We always take steps to support the local communities within which we operate and reach out to the needy by investing in development projects aimed at offering shelter and sanitation to the poor and less privileged at various locations which are discussed under the Social Review on pages 149 to 151.

Although we have not directly financed any major infrastructure development projects this year, our indirect financing by way of disbursements to support infrastructure development and related support, accounts for 5% of total lending.

Refer the below table for total community investment details.

☑ G4-EC 1

MI’s Community Investment Costs for 2016/17

Type of Community Investment	Type of Assistance Given	In Monetary Terms Rs.
Monitory contributions	Financial Assistance and other monitory donations.	1,651,865
Time contributions	4,152 man hours were devoted to enhance the value of societal projects. Employees visited project locations and supported community service initiatives.	1,179,168
In kind contributions	Distributed stationery, sports goods and other educational items to school children. Steel cupboards were donated to a school and an elders' home together with emergency lamps.	393,647
Management cost	848 man hours were spent by some of the corporate management team members, managing the flow of activities related to community project initiatives.	848,000

Management Discussion and Analysis
Relationship Capital Review

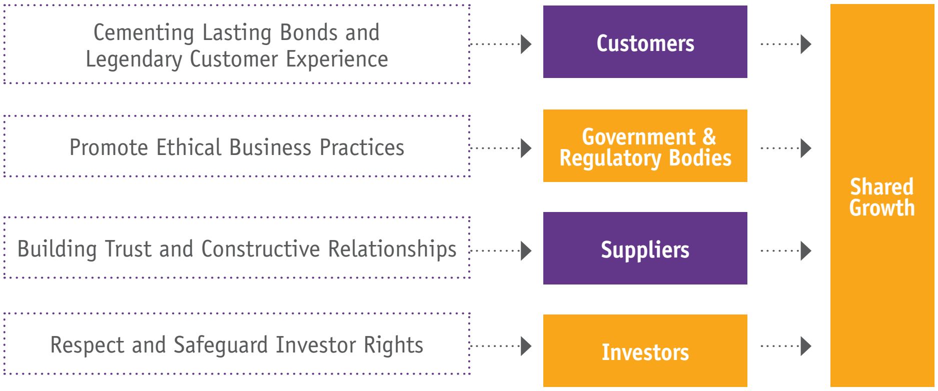
"Many companies describe themselves as customer-focused, but few walk the talk. Most big companies are competitor focused. They see what others are doing, and then work fast to follow. In contrast, MI is driven by what customers want and I have seen the passion and have been lucky to experience a fulfilling business experience".

Patrick Matthew
Customer of Mercantile Investments
and Finance PLC

Overview

Relationship capital is one of the most valuable intangible assets that an organisation has in its value creation process since businesses are driven by relationships. As a premier finance Company which has been in existence for over five decades, MI has built strong and lasting relationships with its stakeholders creating a competitive advantage in a fiercely competitive industry. For MI, Relationship Capital enhancement has come in the form of "Shared Growth" where we have cemented strong relationships which have been mutually beneficial and have brought about a win-win situation for the Company as well as the relevant stakeholder.

Relationship Capital Building Model



http://mi.com.lk/value-creation/value-creating-sixcapitals/relationship-capital/

Relationship Capital - Customer Review

Capital Objectives

- Through receptiveness, identifying solutions to meet growing customer expectations
- Offering a legendary customer experience
- Cement lasting bonds with customers

Future Goals

- Diversify the product portfolio with innovative non-traditional financial solutions
- Widening the customer outreach beyond the Western Province
- Strengthening customer relationship management through decentralisation

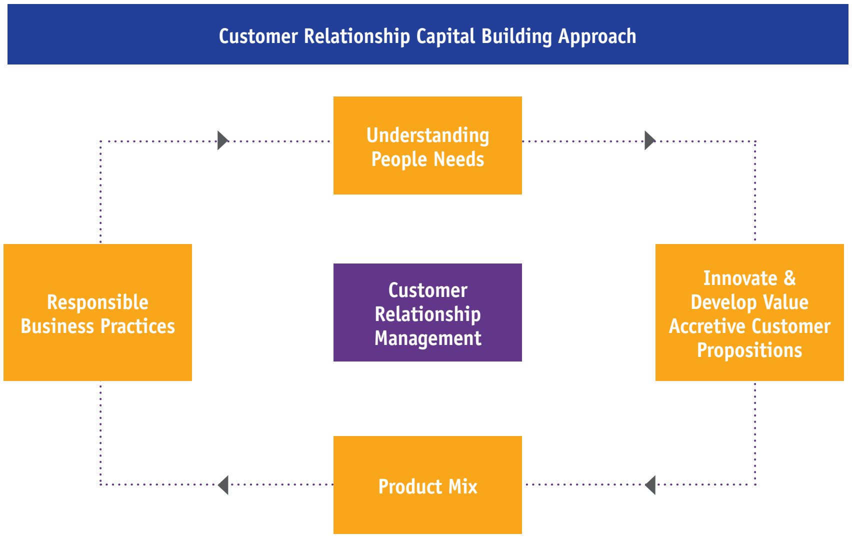
☑ G4-DMA

Our Approach to Customer Relationship Capital Value Building

Building relationships with customers is fundamental for the long term success of any business, and is one of the most influential driving forces of our Company's value creation process. Acquiring and retaining loyal customers for a service providing Company such as ours is typically a challenge, especially in a dynamic and fiercely competitive business environment. However, MI has successfully driven its business to greater heights for over five decades of business excellence, building strong and mutually beneficial relationships with customers, and today these strong customer relationships constitute an integral part of our intangible assets that are a key value driver of our business. Currently both the credit and deposit mobilization arms of the business work closely with our marketing arm to nurture customer relationships as a centralised operation, but would transform to a more decentralised approach in the foreseeable future. Both human resources and technology advances will play a major role towards this endeavour.

Key Performance Indicators

	Actual 2016/17	Actual 2015/16	% Change
New Products Launched	2	3	-33%
New Branches Launched	5	5	-
Growth in Overall Loan Book	14%	29%	-15%
Growth in Deposit Base	8%	15%	-7%
Customer Base	48,884	37,285	31%
New Customers	27,131	20,330	33%
No. of Processes Streamlined to Enhance Service Quality	2	2	-



Management Discussion and Analysis

Relationship Capital Review

Understanding People Needs

For us understanding our target customer base and their needs is vital to build and sustain profitable customer relationships and this has been achieved over the fifty plus years of our existence by being able to deliver service excellence as part of our value offering to our customers. We endeavour to exceed their expectations. The rapid advancement of digital platforms and supporting technology evolving macro and micro economic policies that are subject to frequent change and rapidly developing regulatory frameworks together with other social perceptions have made significant impacts on customer behavioural patterns, expectations and needs. Economic progression of the country and increasing per capita incomes have led to lifestyle changes across all social strata. We as an organisation, have devoted our resources, time and effort to analysing and understanding changing customer behavioural trends, the wants and partially or unmet needs of our existing customers as well as our potential customers to obtain the required insight in crafting our strategies, in segregating our target markets and designing customer centric value offerings that are both innovative and cost efficient. Our solutions and value offerings are driven by customer needs and customer expectations.

We have come to understand that gathering quality customer information on a timely basis and analysis of such information to produce actionable business intelligence is imperative in delivering a customer centric value offering and striving for service excellence with a view to bridging the gap between what the customers expect and what we deliver. This awareness has resulted in the conducting of customer surveys to obtain regular feedback from our customers and the market in understanding their evolving needs and preferences as a primary tool that aids our strategic planning process. The varied customer engagement methods mentioned on page 41, and the feedback on our customer surveys given on page 146 continue to provide valuable insight towards innovation and customer centricity which are vital in crafting customer retention and acquisition strategies that are vital in supporting continued sustainable growth and profitability of the Company in the long term.

Innovation and Development of Value Accretive Customer Propositions

We have forged several strategic initiatives to understand market dynamics and to develop and improve our value offering to fulfil the varying financial needs of our different market segments. Understanding customer needs and aspirations allows us to serve customers with our varied, differentiated and diversified product portfolio and service quality in transforming our customer relationships into a sustainable competitive advantage. We also tailor made our lending propositions that are both traditional and non-traditional to suit customer budgets and preferences; affording step up and structured lease and hire purchase financing and other tailor made repayment solutions, and were successful in offering our customers the convenience from the concept of being a “one-stop” financial service provider offering both lending and deposit mobilisation services. While diversifying our product mix to suit the customers growing needs we always strive to differentiate our product through our superior service to surpass customer expectations. We always give priority to treating our customers fairly by safeguarding customer deposits, ensuring customer satisfaction, retaining their trust, valuing their loyalty and treating customer specific information with confidentiality.

Enhancing Customer Satisfaction

In keeping to our tag line “service that extends beyond”, we work hard to ensure our staff is constantly focused on customer needs and satisfaction. We aim to exceed expectations in terms of service delivery and execution, to be the best. We continued to look for ways to deliver convenience and comfort to our customers as a strategy, actively responding to their growing preferences. Refer service differentiation strategy on page 71 and ancillary value building on page 72 for more details.

We have expanded our branch network comprising of 36 branches/service centres covering key strategic locations, which has extended our customer reach and increased customer convenience. On the other hand, the Company has invested sufficiently in recruiting a knowledgeable and skilled workforce to deliver service quality. MI takes pride in delivering a speedy one day service for all customers in fulfilling their varying financial needs. During the year, we have moved towards more sophisticated and efficient payment modes such as electronic fund transfers and SLIP payments for both deposit and lending advances as a means of strengthening our service excellence and customer convenience. Furthermore, we have advanced our micro collection process this period, through the use of Point of Sale (POS) systems to extend our hassle free service and customer convenience to the micro segment. Currently we are planning to tie up with service providers to offer ATM facilities which will increase the convenience factor for our customer base.

Safeguarding Corporate Trust and Valuing Loyalty

Being a responsible corporate citizen, we expect employees to conduct their activities with integrity and ensure that ethical standards are complied within the course of business operations at all levels of the corporate hierarchy, in keeping with MI's corporate values. We believe that our corporate culture of treating customers fairly plays a vital role in protecting our long standing image and will complement our Brand identity in attracting new customers and building loyalty of our existing customers. Our employees are expected to strictly comply with the Company's policies and procedures and ensure that the embedded manual and system driven controls are robust and working effectively in carrying out their day-to-day operations. Furthermore, our corporate governance and risk management frameworks act as a safety net ensuring that our customers rights and monies deposited with us are safeguarded at all times. Our regulatory compliance underlines all of the above in providing our customers with peace of mind. Our recruitment process is geared to attract individuals who possess the required capabilities and the right character that include the required integrity and professionalism to fit into the working culture at MI. Furthermore, we have strengthened our ICT system with effective controls and safeguards to ensure trust and confidentiality. We uphold product responsibility requisites and conform to best industry practices in this regard. Refer product responsibility on pages 106 to 107 for more details.

☑ *G4-DMA, Sector Specific*

Our Products

Product Mix

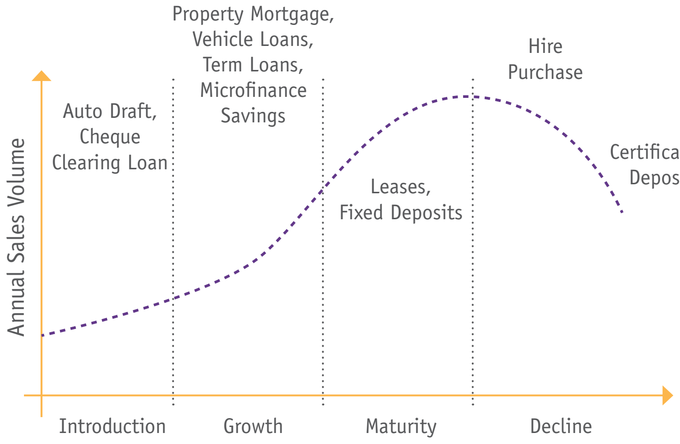
Being a financial service provider, MI offers innovative financial solutions tailor made to our customers' requirements. MI has diversified its lending product range from providing traditional lease and hire purchase financing to term based lending such as personal and corporate loans, pledge loans, property mortgage loans, microfinancing, etc. During the year, several initiatives were undertaken to further enhance our service and the product offerings which paved the way to better fulfil varying financial needs of our customers. Our total product portfolio detailed on page 34 has widened over the years with two new introductions taking place in 2016/17, which is the Auto Drafts and Cheque Loans Products.

Social and Environmentally Benefiting Products

When formulating our product portfolio, our concern extends beyond the commercial boundaries with regard to the social and environmental impacts of our value offering. Our microfinance, Riya Diriya products were aimed at extending financial support for the low income earners with little or no access to alternative methods of financing while contributing to the growth of the agricultural sector. Our expertise and innovativeness has paved the way for us to cater to a vast segment of society as reflected in the analysis based on product, region, value and sector information that is given on pages 92,93 and 136.

Having identified the importance of preserving our natural capital and minimising our indirect environmental impact, our credit identification process is geared in financing more environmentally friendly products such as hybrid and electric vehicles. The expansion of our green lending portfolio is given on pages 136 to 137.

Product Life Cycle



Management Discussion and Analysis

Relationship Capital Review

Finance Leases

Overview

Finance leases being our traditional and the most popular product in our portfolio represents 39% of our total lending portfolio. Our success story of over fifty years is built around the two traditional products of leasing and hire purchase. Although we have expanded our product portfolio to suit the customers growing needs, leases remained the most popular product for MI mirroring its popularity in the finance sector. MI offered a range of leasing services tailor-made to suit the customer needs from private and commercial vehicles to three wheelers and agricultural equipment.

Strategic Focus

We strived to differentiate our lease product through our service excellence where we have minimised our processing time to expedite on the service delivery. While focusing on our hassle free service we also followed a competitive pricing strategy that is derived from sourcing lower rated funds. Our support services on value building, which includes providing in house comprehensive insurance packages and repair and maintenance services offered through our workshop has also contributed to differentiate our product in the market. Furthermore, we strengthened our partnerships with our long-standing vehicle suppliers, agents and customers while focusing on building new relationships. However, as a responsible finance corporate, we were more concerned on the asset quality as well as the recoverability of our portfolio in minimising our overall business risk. We worked closely with those borrowers facing financial difficulties, to recover and reschedule repayments towards regularisation by refinancing and restructuring their debts which totalled Rs. 284 Million this period. (2015/16 Rs. 227 Million).

Future Outlook

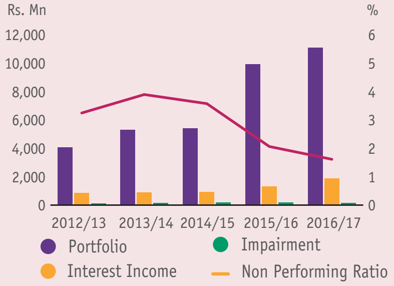
MI's forecasted lending growth expectations for the medium term have been set bearing in mind the fierce competitive market and fiscal and monetary policy changes. Due to the limitations of 50% LTV on lease vehicles remaining the most significant challenge, we will focus more on financing registered vehicles. We hope to extend personalised customised service expanding our reach and identifying the exact needs of the existing and potential customers and providing the optimum solution to suit their needs.

Performance

Customer Inclusiveness - Leases

Our focus on our legendary customer experience and the unparalleled service has attracted new customers while satisfying the needs of the existing customers. During the year the leasing customer base reported a growth of 17% with the new customer acquisitions being reported at 28% of the total leasing customer base.

Portfolio Dynamics - Lease



Although the leasing business was restricted due to limitations imposed on the LTV ratio, and continued increase in vehicle prices due to increases noted for import duties and in world prices, we succeeded in achieving a moderate growth of 12% in the lease portfolio in 2016/17. Our focus on registered vehicles and the expansion of the branch network, along with our service excellence were key drivers of growth. Despite recording moderate portfolio growth for leasing in FY 2016/17, our income nevertheless improved significantly by 42% mainly due to the continuous revisions that we made to product pricing.

Even though the industry statistics reflected increased levels for Non-Performing Loans (NPL) with an increased credit risk, the Company's low Risk Appetite and stringent recovery efforts resulted the NPL for leases remaining below 2%. Accordingly, the leasing impairment charge dropped by 153% year-on-year, while the product provision cover remained at a satisfactory 86%.

Hire Purchase

Overview

The Hire Purchase (HP) business vertical which was MI's leading product in the past, experienced a decline due to the rise in popularity of non-traditional forms of lending such as personal loans, property mortgaged loans, etc., and also due to the elimination of VAT on leases, making leases more attractive. We identified potential to develop the hire purchase business vertical, focusing on older vehicle segment, but noted that there was a visible decline in demand overall, unlike in the past.

Strategic Focus

Owing to the decline in demand, we continued to promote hire purchase facilities to specific market segments only, rather than catering to a wider market as done in the past. We customised our hire purchase offering to targeted segments having evaluated ways in which to deliver convenience and ease of doing business to our customers, actively responding to their growing preferences. MI offered tailor made structured hire purchase agreements based on customer need, repayment capacity and convenience.

Future Outlook

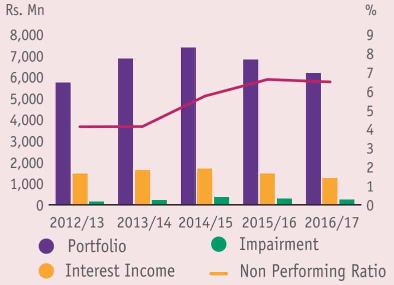
Although the demand for hire purchase financing is bound to gradually decline, MI will continue to promote the product beyond the Western Province, focusing more on registered vehicles with the expectation of retaining the overall market share.

Performance

Customer Inclusiveness - Hire Purchase

In the backdrop of declining popularity, our total hire purchase customer base contracted by 8% while the new customer acquisitions stood at 22% of the total hire purchase customer base.

Portfolio Dynamics - Hire Purchase



Despite the hire purchase portfolio remaining between the mature and declining stages of the product life cycle and the total portfolio declining, income from hire purchase was reported at Rs. 1,263 Million, but this too reflected a decline of 13%. Hire purchase NPL ratio and impairment charges too remained at relatively lower levels.

Management Discussion and Analysis

Relationship Capital Review

Loans and Advances

As a non-traditional product line, this consists of a variety of products with varying yields which are based on their respective risk levels and pricing strategies. Offering a diverse range of products enabled us to cater to varying customer requirements, while the Company benefited from higher volumes and higher yields. By introducing the two new products to our loans portfolio, we satisfied additional customer segments. Vehicle loans, property mortgaged loans, term based lending and microfinance loans were the main products which contributed 99.5% as interest income to total loans and advances revenue.

Vehicle Loans

Overview

With the evolution of customer demands and preferences, our traditional lending products of leasing and hire purchase are being gradually overshadowed by vehicle loans which offer customers the opportunity to own their dream vehicle without incurring any additional tax burden. This product is aimed at financing both registered and unregistered vehicles with the option of structuring the instalments based on customer's repayment ability.

Strategic Focus

We strived to maximise our service excellence to add extra benefits to the customers and to capitalise on our personalised quick service with minimal lead time, differentiating our product from the market. Our customer oriented service focused on creating lasting customer bondage and loyalty which we believe is an influential marketing tool for expanding our customer base and the business.

Future Outlook

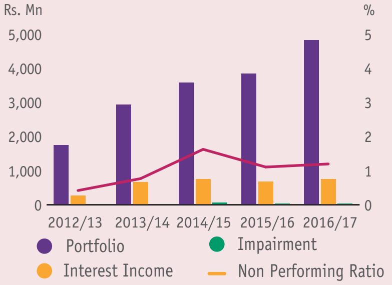
Considering the growing demand for vehicle loans, we have increased our focus towards vehicle loans instead of traditional products, where the customer is entitled to enjoy more flexible and convenient terms based on his requirement which commensurate with the individuals risk profile. We will strive to add more customer oriented product features, while strengthening our hassle free service to expand our market share while adhering to our credit approval process, risk assessment criteria and regulatory compliance.

Performance

Customer Inclusiveness - Vehicle Loans

In 2016/17 our total customer base expanded by 30%, whereas the new customer acquisitions stood at 28% of the total vehicle loan customer base.

Portfolio Dynamics - Vehicle Loans



The total vehicle loans portfolio grew by 25%, while related income growth was at 12%. Despite the portfolio expansion, we were able to maintain the NPL below 2% well controlled due to our stringent recovery efforts on managing asset quality.

Property Mortgaged Loans

Overview

MI offers this product for both individuals and to corporates to purchase, refinance or make improvements to property by mortgaging their assets. The demand for these loans has been gradually expanding with the increase in per capita incomes, population growth and the growing demand for apartments situated in close proximity to Colombo and upcoming suburban regions.

Strategic Focus

Although there was a growing demand for mortgaged loans, we adopted a more conservative approach when expanding the mortgaged loan portfolio, based on strict credit review policy and risk assessment criteria to minimise the overall credit risk. However, as an ongoing strategy we are moving towards expanding our mortgaged loan portfolio within our defined Risk Appetite, as a means of diversifying our product mix and improving our average yields.

Future Outlook

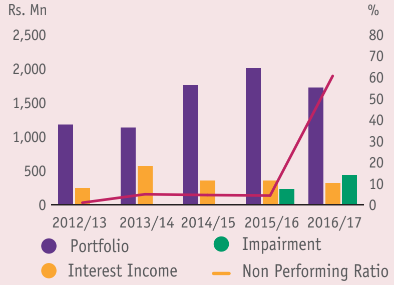
Having analysed the industry statistics, we noted that the demand for property mortgaged loans is increasing in the finance sector creating an opportunity for the companies in the sector to reach their target growth levels in both portfolio and income levels to counter the limitations imposed on LTV and the rise in interest rates. However, we strive to mitigate the risk exposures by setting up single borrower limits and carrying out thorough review of the security, while ensuring credit worthiness of the customer as a pre-requisite, as part of our risk identification and management process.

Performance

Customer Inclusiveness - Property Mortgage

MI's property backed customer base contracted by 7% in 2016/17, as we took a risk averse approach considering the inherent risk and was selective.

Portfolio Dynamics- Property Mortgage



Property mortgage lending and interest income declined by 3% and 9% respectively, since we adopted a more conservative approach with regard to this specific segment, though it contributed to 6% of the total interest income. Although related NPL levels increased on account of few large accounts, the overall asset quality was kept at a favourable level as all such NPL's were fully backed by collateral. However, in line with Sri Lanka Accounting Standards (LKAS/SLFRS) requirements, we recorded Rs. 434 Million as impairment provision for respective problematic accounts.

Management Discussion and Analysis

Relationship Capital Review

Term Based Lending

Overview

We provide credit facilities for all legitimate needs and have a diverse product range to support varying customer needs. This includes personal loans, professional loans and other term loans. During the year, we introduced a new revolving credit facility (Auto Draft) to our existing customers with good credit scores and repayment track records, and introduced Cheque Loans, a form of clean lending, offered to a selected customer base who has demonstrated over time that they are credit worthy and financially sound.

Strategic Focus

With the increase in market competition and the varying customer needs, we have identified that there is a growing demand for products where the customers are allowed to serve only the interest at each month end and the principal at the maturity, which offers additional benefit to manage their cash flow requirements. Considering the prevailing economic conditions and the interest rate volatility MI has placed more focus in promoting this form of lending with the option of selecting either fixed or variable interest rates.

Future Outlook

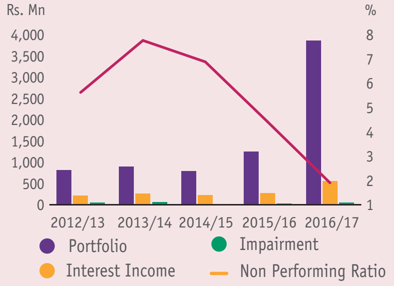
Since MI intends to further diversify its product mix through non-traditional product lines, more focus would be given to expand this type of term based lending by introducing new product features, facilitating new customer preferences and tailor-made repayment plans. At the same time we expect to create a competitive edge, by delivering a personalised service experience utilising the growing branch network to our advantage.

Performance

Customer Inclusiveness - Term Loans

With the expansion of our product mix and the branch network, MI was able to achieve 163% growth in related customer base whereas the new customers stood at 27% of the total term loan customer base in 2016/17.

Portfolio Dynamics - Term Loans



Although overall growth in our total loan book grew at a lesser pace, we were able to achieve a noteworthy growth of 211% from term loans in 2016/17. Since LTV limitations on lease and hire purchase lending created demand for other funding methods, we were able to capitalise on this opportunity, developing both the existing portfolio and new products. Despite the portfolio expansion, we were able to maintain the NPL ratio below 2% due to our stringent recovery efforts and credit evaluation process which enabled the Company to maintain asset quality levels.

Microfinance Based Lending

Overview

MI's Microfinance lending is targeted at the low income earners who have little or no access to alternative methods of financing. Our microfinance loans and consumption loans support the lives and livelihoods of the rural population living outside the Western Province. During the year, the Company was able to accelerate microfinance lending through the efforts of the micro division set-up in the previous financial period consisting of experts in the field of microfinance.

Strategic Focus

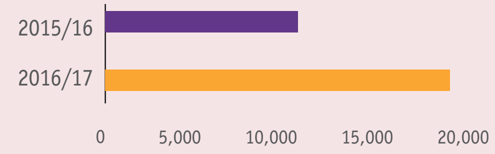
By setting up a microfinance divisional unit at branch level, with specialised and experienced staff, our strategy throughout has been to increase customer access to payment centres providing microfinance. Our strategy focused on extending these facilities to women, who have become a driving force in this sector. By introducing the Point of Sale (POS) systems from this period, we have made the collection process hassle free and convenient to the customer. Furthermore, we have introduced more value accretive features such as the provision of in-house insurance cover and the reimbursement of funeral expenses in the event of death, as an extra benefit to the customers.

Future Outlook

As a socially benefiting product, we hope to expand our reach for microfinance based lending, to cater to a wider cross section of the population across various regions and communities in the country. We will further strengthen our team while expanding our branch network, extending the microfinance based lending through all our existing branches. As a part of a "Shared Growth Proposition", we encourage communities to improve their savings habits and to develop their living standards through self-empowerment strategies.

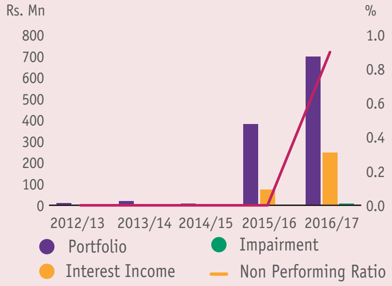
Performance

Customer Inclusiveness - Microfinance



Our aggressive strategy has enhanced our customer base by 90% in 2016/17 alone, bringing the total number of customers to 17,954.

Portfolio Dynamics - Microfinance



Our microfinance portfolio growth stood at 86%, mainly fuelled by the addition of microfinance units at branch level and also due to the introduction of the microfinance consumption product and enhancing of microfinance limits. Despite the high risk involved with microfinance lending (being a clean facility), we were able to maintain the NPL ratio below 1% through the weekly collection process and credit evaluation skills used to assess creditworthiness.

Management Discussion and Analysis

Relationship Capital Review

Deposits - Fixed Deposits

Overview

With over five decades of trusted service, MI is viewed as one of the most trusted Licensed Finance Companies (LFC), garnering confidence amongst investors for the provision of deposit mobilisation services in Sri Lanka. Fixed deposits make up a significant 99.7% of the Company's Rs. 17 Billion deposit base and the numbers have been increasing significantly over the years.

Strategic Focus

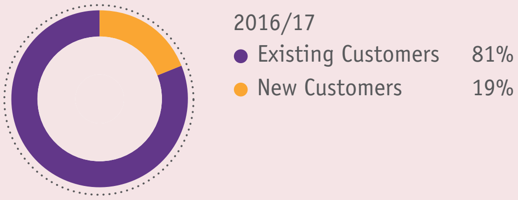
Growth in fixed deposits remained a key priority for MI as a funding source, and a gateway to building lasting customer relationships. We stayed committed in building our deposit base, amidst the fierce competition faced from banks and other finance companies within the industry, offering competitive rates. While focusing on attracting new customers through our branch network, MI took a two pronged approach of also focusing on retaining our existing loyal customers through service excellence, by leveraging on relationship management skills and the trust and confidence built from safeguarding their investments over time. During the year we also streamlined our internal processes and widened the payment options to enhance customer convenience. Furthermore, we endeavoured to increase the long term deposit base to reduce our short term assets and liability maturity mismatch.

Future Outlook

Sustaining a well balanced deposit base will be crucial for us, in providing the necessary funding support to stimulate the forecasted growth in lending. In the midst of a tight monetary policy that would continue to result in gradual hikes in interest rates, MI would strategise to mobilise cheaper longer term deposits in order to safeguard interest spread levels. We will further strengthen our branch network with more human resources and technology developments since our branch network would play a pivotal role in mobilising retail fixed deposits. Furthermore, we are currently planning greater decentralisation to further strengthen our strategy driving customer convenience.

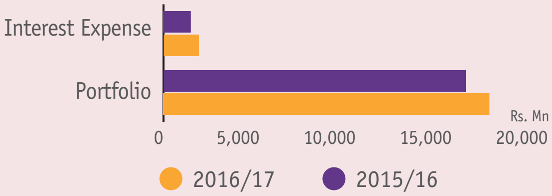
Performance

Customer Inclusiveness - Fixed Deposits



Our fixed deposits customer base has increased by 7% in 2016/17 since we were able to expand deposit mobilisation services through our branch network.

Portfolio Dynamics - Fixed Deposits



We were successful in attracting fixed deposits from various segments that included deposits from individuals and corporates with the total deposit base for fixed deposit amounting to Rs. 17 Billion. Although, our expected growth was curtailed due to the volatility in interest rates and rigorous competition, we sustained repeat business through the Company's loyal depositor base, and also attracted new depositors through our growing branch network, given the Company's premier status in the LFC sector.

The total fixed deposit interest expense increased by 29% year-on-year and was driven not only by the growth in the total deposit base but also due to the re-pricing effect from increasing interest rates.

Deposits - Savings Deposits

Overview

Inculcating the important habit of saving amongst the masses of Sri Lanka, we offer MI Max Savings Account and MI Kids Savings Account with attractive interest rates. However, these products remain in their nascent stage and at the introduction level of the product life cycle. The future potential of these products will be harnessed with time through focused marketing and distribution strategies.

Strategic Focus

Our personalised customer service which includes a combination of doorstep services, flexible terms and attractive interest rates endorsed our service differentiation strategy to create an unparalleled level of customer satisfaction. MI's deposit marketing arm worked closely with the branches in building brand loyalty and continued to create awareness; especially beyond the Western Province.

Future Outlook

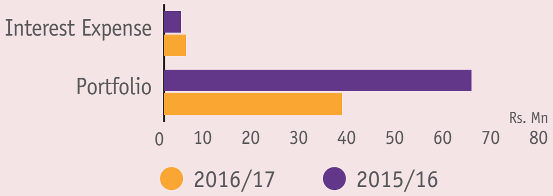
The Company will pursue to develop the savings deposit business through our strong branch network while strengthening the deposit arm in each branch with additional human and technological resources. We will maximise our investments in ICT to support the robust service initiatives to the fullest in 2017 and 2018 by focusing on improving the productivity and efficiency of the business, in addition to driving customer convenience in facilitating same day payments through e-payment solutions and ATM support.

Performance

Customer Inclusiveness - Savings Deposits

MI was able to expand the savings customers by 6% in 2016/17. A much steeper rise is forecasted for the next year with the introduction of ATMs which was identified as a customer need.

Portfolio Dynamics - Savings Deposits



With the stringent competition in the market and contracting economic growth, savings deposit portfolio in value contracted by 42% at the end of 2016/17, although there was a considerable portfolio growth during the middle of the year, resulting in the interest expense increasing by 29%.

Management Discussion and Analysis

Relationship Capital Review

☑ *G4-14*

Responsible Business Practices

As a responsible finance company, we are committed in inculcating ethical business practices and ensuring the transparency and accountability of our products and services.

Product Responsibility

As the business of finance revolves to a great degree on trust and confidence, for MI it is of paramount importance that we conform to required product responsibilities towards our customers, other related parties and the general public. By laying down clear operational policies and procedures for our lending business and for deposit mobilisation, and strengthening compliance through the process of training, the Company expects all back-office and front-office staff who deal with product handling, to strictly comply with all such requirements. These procedures, rules and regulations will ensure anticipated service standards are extended to our customers, and the Company does not fall short of our product responsibility duties and obligations. Technology plays a supporting role in this process, helping to safeguard large amounts of confidential data from being accessed by intruders through inbuilt control mechanisms.

Product Responsibility Policy

In order to provide a fulfilling product that will yield maximum satisfaction to our customers, we expect to extend a professional service that will fulfil our product responsibility obligations. The product policies, practices and standards embraced have been developed with due care, taking into consideration regulatory obligations and industry practice, whilst also ensuring MI continue to be fair competitors in the market. All our marketing communication activities conform to the highest levels of integrity and honesty, in a socially acceptable manner and do not in any way resort to or condone unethical communications to mislead the public.

☑ *G4-FS 8*

Management Responsibility and Audit of Products

Responsibility for the overall management and adherence to product related requirements lies with the respective core divisional heads of lending business and deposit mobilisation business, under overall leadership of the Managing Director and the Board. The heads and their staff maintain required standards at all times complying with various operational instructions specified in respective operational procedure manuals. These cover key requisites in relation to product development, product handling, product delivery, marketing and communication, record keeping, product monitoring and compliance. Regular reviews are carried out by the internal audit team which cover MI’s adherence to product responsibility requirements in relation to both lending and deposit businesses. Audit coverage also includes environmental and social policy review.

Product Goals/Targets

In extending “a service that extends beyond“, we understand the importance of setting product targets to reach excellence, considering the growing preferences of people, which keeps changing and widening at a rapid pace. Therefore, we strive constantly to maintain excellence in product service standards and enhancing our product range to meet growing expectations of people. The Company continued to extend an attractive wide-ranging product mix, tailoring financial services at times to meet customer preferences. Core business units were asked to maintain challenging business volumes and transaction levels and some of these targets were monitored by the finance department and presented to Executive Directors and senior management on a weekly basis. In parallel, respective core departmental heads continued to review their staff's performance against set sub-targets.

Product Handling Knowledge

Continuous training was provided to employees handling products, by enhancing their technical knowledge and other basic skills. As part of MI’s learning environment, employees attached to core business divisions were given in-house training either desk learning or on-the-job-training on various operational requirements, procedures and processes, which ensures there is effective product handling by the respective officers, so that product responsibility requirements of the Company are fulfilled.

☑ *G4-DMA, PR 6*

Responsible Marketing and Communication

We want our customers to understand their financial portfolios and to extend our support to select the most suitable financial solution based on their need. That’s why MI embeds responsible design, marketing and education into our suite of products and services. Our marketing and branding strategy has been designed in line with the said objectives, going beyond all statutory and regulatory compliance requirements. All our marketing communication activities that include advertisements and promotional campaigns are carried out, reflecting true facts with responsibility, and are carried out in an ethical manner. In keeping to regulations, required advertisements and communiqués in relation to deposit mobilisation is forwarded to the regulator and necessary approval obtained prior to its release. We do not deal in promotion of banned or disputed products and products that are subject to stakeholder questions or public debate. The marketing and communication methods explained in page 70 under strategy were carried out in a responsible manner. To maintain a greater level of accountability, we strive to make all communications as transparent and focused as possible.

Monitoring of product performance

There is close monitoring of the performance of all product categories by the respective core divisional heads and the Executive Directors. Directors and members of the corporate management meet weekly to review performance and in such meetings actual product performance is measured and compared against targeted goals. As part of the monitoring process, success levels of product market strategies implemented are also monitored by the senior management to ensure organisational goals have been fulfilled to expectation. During such evaluations, appropriate revisions were made to implemented product strategy to ensure continued viability of our product lines, to sustain competitive advantage. Pages 98 to 105 describe our product strategy and the resultant financial performance of each key product for the period under review.

Product Responsibility Performance Indicators

☑ *G4-DMA, PR 1, PR 2*

Customer Health and Safety

There is no direct health and safety risk arising for our customers from carrying out a finance business operation from any of our locations. Nevertheless, as a responsible corporate we ensure that whatever health and safety risk that may prevail is minimised and managed for all those who visit MI Head Office premises and our branch network. Required safety procedures have been established to secure the health and safety of all our customers. The Security Coordinating Officer is entrusted with the responsibility of looking after the overall security of employees, customers and others visiting the offices. For this purpose, effective security measures are in place that includes close monitoring of people by security officers stationed around MI premises. CCTV facilities have been utilised across the branch network to enhance security monitoring.

☑ *G4-DMA, PR3, PR5*

Product and Service Labelling

We adopt industry accepted documentation formats to execute our business transactions with customers. There is adequate product related information provided for and these documents include lending agreements, guarantor documents, deposit certificates, etc. Terms and conditions are given for the understanding of contracting parties and clear agreement clauses have been specified that are industry accepted and fair.

Key transaction documents with clauses - Visit MI website.

http://mi.com.lk/value-creation/value-creating-sixcapitals/relationship-capital/

Mostly a common logo is used for MI's brand development and promotion of the product range across the country. Based on the requirements arising from the language policy regulations, our key agreements have been made available in all three languages-English, Sinhala and Tamil, at MI operational points.

The newly setup Related Party Transaction Review Committee reviews related party transactions carried out during a period. The Committee carries out this assessment to establish that such transactions have been done on an arm's length basis and that there is no conflict of interest taking place at Director level with any of the transacting parties. We also monitor customer satisfaction levels through a general survey (Refer customer survey results on page 146).

☑ *G4-DMA, PR 8*

Customer Privacy

Maintaining confidentiality of large amounts of customer information that is placed before the Company on a day-to-day basis, is of paramount importance. The information security policy document that has been approved by the Board highlights the importance of protecting customer information from intruders and therefore, has placed stringent internal procedures and rules for both IT staff and users. The Company has therefore, established an effective information security control environment with required inbuilt system controls as well as other physical and external controls. Required controls have also been inbuilt to all ICT systems operated and as a practice whenever we acquire new information technology solutions or make changes to existing platforms, we ensure adequate controls are set-up to ensure confidentiality of data. There are numerous security features embedded in the core information system such as system passwords to limit access, automatic backing up of data, virus protection, firewalls, etc. We did not come across any reported breaches of customer privacy, during the period under review.

Handling Customer Complaints

We have well trained staff to assist our customers in resolving any problem. We strive to provide an immediate solution to resolve any customer concerns. However, if more time is needed to resolve a problem, we feel it is vital that we "Go that extra mile for the customer" and provide a concrete solution to the issue in question. There have been no complaints of any unresolved critical issues during the reporting period. All customer inquiries regarding business operations have been successfully resolved at the respective unit-level itself.

☑ *G4-PR 2, PR 4, PR 7, PR 9*

Product Compliance

During this period, there were no significant fines against the Company for non-compliance with laws and regulations concerning the provision and use of products and services including aspects related to product information and labelling. Further, there have not been any incidents of non-compliance with regulations concerning health and safety impacts of our products and services. There were also no reported incidents of non-compliance with regulations concerning marketing communications.

Management Discussion and Analysis

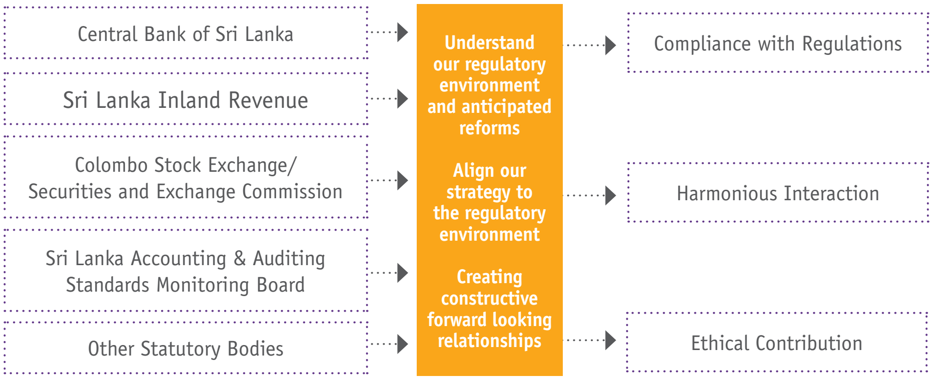
Relationship Capital Review

Relationship with Regulatory Bodies

Due to the nature of our business and operating in a highly regulated sector, maintaining cordial relationships and winning the trust of regulators by being compliant with laws and regulations is vital for a sustainable value creation process. MI, as a responsible premier finance company has always strived to achieve a standard of compliance which exceeds the mere legal requirements and embraces best-in-class practices within the industry including applicable global best practices. We always endeavour to conduct our operations in an ethical manner consistent with stakeholder interests and aspirations including those of the regulatory authorities.

The need to be compliant comes naturally to us based on our overarching culture of prudence. The need to be compliant gives way to the Company having formal governance and risk frameworks institutionalised at all levels of the hierarchy. Having a Compliance Officer gives further credence to our need to be compliant with all applicable regulations, directives and laws. During our business journey, we have understood the value of being compliant as a responsible provider of financial services. We approach compliance with professionalism and responsibility and as such it has led to building cordial relationships with all regulators having earned their trust.
We continue to maintain cordial relationships with the following regulatory bodies.

Regulatory - Relationship Capital Value Building Process



Central Bank of Sri Lanka

Sri Lanka Inland Revenue

Colombo Stock Exchange/ Securities and Exchange Commission

Sri Lanka Accounting & Auditing Standards Monitoring Board

Other Statutory Bodies

Understand our regulatory environment and anticipated reforms

Align our strategy to the regulatory environment

Creating constructive forward looking relationships

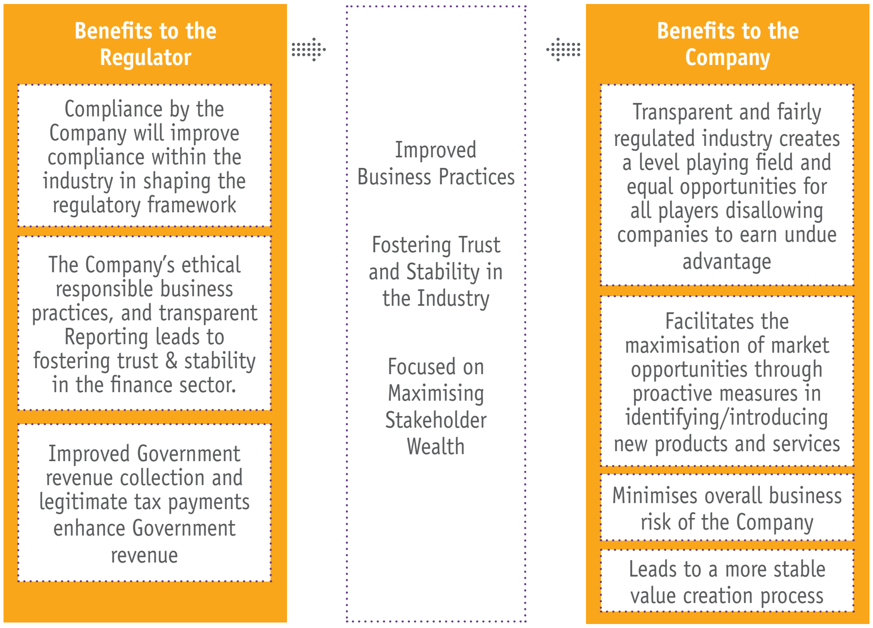
Compliance with Regulations

Harmonious Interaction

Ethical Contribution

Statutory Requirements	**2016/17**	**2015/16**
Liquid Assets (minimum 10%)	10.81	11.73
Core Capital Ratio (minimum 5%)	17.17	19.35
Total Risk Weighted Capital Ratio (minimum 10%)	14.26	15.75
Taxes Paid to the Government (Rs '000)	226,703	460,043
Tax Savings/Credits Received	36,589	11,261

Value Balance between Regulators and MI



Benefits to the Regulator

Compliance by the Company will improve compliance within the industry in shaping the regulatory framework

The Company's ethical responsible business practices, and transparent Reporting leads to fostering trust & stability in the finance sector.

Improved Government revenue collection and legitimate tax payments enhance Government revenue

Improved Business Practices

Fostering Trust and Stability in the Industry

Focused on Maximising Stakeholder Wealth

Benefits to the Company

Transparent and fairly regulated industry creates a level playing field and equal opportunities for all players disallowing companies to earn undue advantage

Facilitates the maximisation of market opportunities through proactive measures in identifying/introducing new products and services

Minimises overall business risk of the Company

Leads to a more stable value creation process

Understanding our Regulatory Framework and Anticipated Reforms

Understanding our regulatory environment is a key element in formulating our business strategies which lays the foundation for sustainable value creation to take place. We have established a separate risk and compliance unit, which ensures that the effects of all the existing and new regulations are duly communicated and implemented in a timely manner as intended. Through continuous training and development programmes, we ensure that our employees keep abreast of the changes to the regulatory framework, and obtain requisite expertise and professional advice as necessary.

Align Our Strategy to the Regulatory Environment

As a responsible corporate citizen, we are committed in maintaining the highest levels of compliance, institutionalising ethics in all areas of our business. We continuously monitor and identify regulatory requirements and establish appropriate policies and procedures, in conjunction with the compliance officer to meet with product responsibility requirements. (Refer pages 106 to 107 on product responsibility). Our strategic goals have been developed in line with regulatory requirements which ultimately ensure that we meet with our capital adequacy ratios together with our products and services which comply with all applicable laws and regulations.

Creating Constructive Forward Looking Relationships

In our journey towards sustainable value creation for all our stakeholders, we have identified that it is vital to enhance our constructive relationship with all the regulatory bodies. In doing so it enables the Company to strike a balance between diverse stakeholder needs and expectations.

✓ *G4-EC 4*

Financial Assistance received from Government

No direct investment has been made by Government bodies in shares of MI and no direct funding arrangement made towards MI during the year.

Key CBSL regulations imposed in 2016/17 applicable to LFC's

Directions	Key Requirements of the Direction	The Company's Status of Compliance
Loan to Value Ratio for Loans and Advances Direction No. 3 of 2017	Specifying maximum limits of Loan to Value ratio for all vehicle backed lendings. a) Commercial vehicles 90% b) Motor Cars/Vans 50% c) Three wheelers 25% d) Others 70%	MI has set the maximum limits in granting credit facilities in line with the direction requirement
Minimum Core Capital Direction No 2 of 2017	Maintain an unimpaired core capital at a level not less than Rs. 400 Million until 31.12.2017, and thereafter, maintain the core capital level at a level not less than the amounts stipulated below. a) Rs. 1 Billion by 01.01.2018 b) Rs. 1.5 Billion by 01.01.2019 c) Rs. 2 Billion by 01.01.2010 d) Rs. 2.5 Billion by 01.01.2021	The Company's strong capital base is well above the minimum core capital requirement

Management Discussion and Analysis

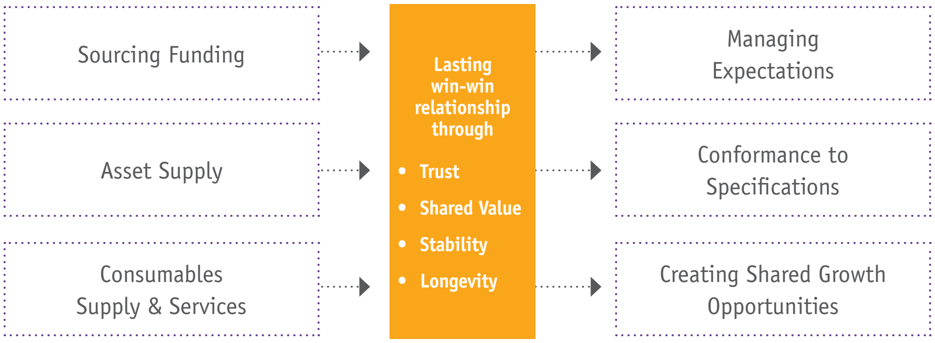
Relationship Capital Review

Relationship Capital - Supplier Review

Building lasting and constructive business relationships with suppliers is a key aspect for the Company in gaining competitive advantage. MI has built strong relationships with its suppliers through mutually rewarding partnerships. Our long-standing relationships have been built on the "Trust", "Shared Values", "Stability" and "Longevity" in the industry. Our goal is to develop sustainable business partnerships and ensure that our suppliers work in a way that is consistent with our expectations.

Being a service provider, our supplier relationships are built on the following operational lines.

Supplier - Relationship Capital Value Building Process



Sourcing Funding

Sourcing funding is a critical factor in expanding our core business activity of lending. Funds obtained from our key banking partners and financial institutions through short term and long term loans, securitisations and issue of debt security are the main sources of our funding, excluding customer deposits. Maintaining lasting relationship with our lenders will enable us to finance our lending growth at a minimal cost and to offer competitive rates to our customers.

Asset Supply

Property, plant and equipment and other office related items are required to create a well-equipped operating platform and corporate ambiance.

We have created strong bonds with our key suppliers facilitating the obtaining of quality products and services to suit our requirement at reasonable prices.

Consumable Supplies and Services

Although material purchasing is not significant to our business, as a service provider, we require a considerable amount of stationery and other consumable supplies. In dealing with our existing network of suppliers of these items, we ensure that we maintain the appropriate lead times that minimise the inventory pertaining to stationery and consumables, and optimize on costs by ensuring quality supplies.

MI also maintains a separate motor vehicle inventory stock comprising popular vehicle brands supplied from reputed vehicle suppliers.

In addition to the above mentioned suppliers, we maintain sound relationships with our utility providers, media, and consultancy and advisory services in our value creation process.

☑*G4-DMA on Procurement Practice*
EC9 – Supplier Assessment and Spending

Procurement Practices

MI follows a centralised purchasing procedure in purchasing stationary and consumables for the Head Office and branches. We follow a streamlined process to select our registered list of suppliers and this involves an inclusive procurement strategy, where we look to strike the right balance between cost, quality and environment aspects, while at the same time giving suppliers the opportunity to increase their own wealth creation capacity. Our suppliers are reviewed periodically to ensure that the product/service quality, legal and regulatory compliance and the cost effectiveness remain compliant with the requirements of the Company. This enables the Company to compare existing suppliers with upcoming reputed suppliers, giving fair opportunities to all the suppliers. We ensure that our procurement conforms to our required specifications of timely delivery and cost competitiveness. Furthermore, we have strengthened our ICT based inventory system to manage purchases of stationery and consumables as well as other related management information requirements.

Proportion of spending on local suppliers at significant locations of operations - Visit MI website

http://mi.com.lk/value-creation/value-creating-sixcapitals/relationship-capital/

Relationship Capital - Investor Review

Investors are the primary stakeholders who pave the way for the value creation process to take effect, and accordingly our business model encompass various inputs and processes that subject the capital invested by our investors through a transformation process that results in a return on capital that has been sustained over the fifty plus years of our existence. We have always worked to build strong bonds with our shareholders and in doing so; recognise the importance of being ethical and transparent about our activities. Our goal is to maximise shareholder wealth without compromising on other stakeholder expectations and to provide shareholders with a timely, accurate and balanced disclosure of all material information about the activities and progress of the Company. Furthermore, we keep our investors closely apprised of the corporate strategies, actual performance against planned performance, actions to realign with the plan, future forecasts and key strategic issues and risks influencing both the Company and the industry in gaining their trust and confidence in the management of the Company.

Investor - Relationship Capital Value Building Process

Compliance with investor regulations and respecting the rights of investors

Financial Information	2016/17	2015/16
Equity Holders		
Earning Per Share (EPS) - Rs.	67.20	168.00
Dividend Per Share (DPS) - Rs.	-	7
Dividend Pay Share (DPO) - %	-	0.7
Net Asset Value Per Share (NAVPS) - Rs.	2,617	2546
Price Earning (PE) Times	38.39	13.10
Price to Book Value (PBV) Times	0.99	0.86
Dividend Yield (DY) - %	-	0.31
No. of Shares (ooo')	3,006	3,006
Share Capital (Rs. Mn)	30.06	30.06
Total Equity (Rs. Mn)	7,867	7,654
Total Financial Liability (Rs. Mn)	29,053	25,808
Core Capital Ratio (Minimum Statutory Requirement 5%)	17.17%	19.35%
Total Risk Weighted Capital Ratio (Minimum Statutory Requirement 10%)	14.26%	15.75%
Debt Holders		
Debt to Equity Ratio (Times)	1.43	1.17
Interest Cover (Times)	1.1	1.38
Current/Quick Ratio (%)	10.81	11.73

Shareholder Wealth Accretion

The Company's strategy on shareholder wealth accretion is geared through a moderate risk profile generating sustainable returns, while ensuring shareholder trust and confidence is safeguarded at all times. In keeping with corporate aspirations of realising steady investor returns year-on-year, the Company was able to record satisfactory profitability levels for the financial year 2016/17, amidst challenging market conditions and frequent changes to macroeconomic policy conditions, though behind expected. Year-on-year growth was also reported for revenue, lending and total assets. Our investors over the years have enjoyed sound returns in terms of dividends and have seen their investments grow through a constant accumulation of shareholder funds that now stands in excess of Rs. 7.8 Billion. As a result of this strong and growing net asset position, MI's ordinary share market price remains exceptionally high. Based on the last recorded trade upon listing, MI shares traded at Rs. 2,580.30/- per ordinary share. The Company's net asset value per share has gradually increased over time, while however dividend payout had been moderate until this year where it is nil, mainly due to the strong policy of retaining funds for future growth.

Management Discussion and Analysis

Relationship Capital Review

Stock Exchange Listing

The issued ordinary shares of Mercantile Investments and Finance PLC are listed in the Diri Savi Board of the Colombo Stock Exchange. The audited Income Statement for the year ended 31st March 2017 and the audited Balance Sheet of the Company as at that date have been submitted to the Colombo Stock Exchange.

Stock exchange code for Mercantile Investments & Finance PLC share is "MERC".

MI's Investor Base

The Company's investor base currently comprises of 3,006,000 voting shares distributed among few large investors as given in the table below. The total numbers of shareholders reduced to 17 in 2016/17, whereas in the previous year there were 19 shareholders. There were no non-voting shares issued by the Company or any changes in share capital of the Company during the year.

Distribution of Ordinary Shareholders

As at 31st March 2017	Resident			Non-Resident			Total		
	No. of Share holders	No. of Shares	%	No. of Share holders	No. of Shares	%	No. of Share holders	No. of Shares	%
1 - 1,000	3	1,153	0.04	1	10	0.00	4	1,163	0.04
1,001 - 10,000	1	2,004	0.07	-	-	-	1	2,004	0.07
10,001 - 100,000	5	55,110	1.83	-	-	-	5	55,110	1.83
100,001 - 1,000,000	7	2,947,723	98.06	-	-	-	7	2,947,723	98.06
Over 1,000,000	-	-	-	-	-	-	-	-	-
Total	16	3,005,990	100.00	1	10	0.00	17	3,006,000	100.00

Analysis of Shareholders

Resident/Non-Resident

	31st March 2017			31st March 2016		
	No. of Shareholders	No. of Shares	%	No. of Shareholders	No. of Shares	%
Resident	16	3,005,990	100.00	18	3,005,990.00	100.00
Non-Resident	1	10	0.00	1	10.00	0.00
Total	17	3,006,000	100.00	19	3,006,000.00	100.00

Individuals/Institutions

	31st March 2017			31st March 2016		
	No. of Shareholders	No.of Shares	%	No. of Shareholders	No. of Shares	%
Individuals	14	1,758,451	58.50	16	1,768,461	58.83
Institutions	3	1,247,549	41.50	3	1,237,539	41.17
Total	17	3,006,000	100.00	19	3,006,000	100.00

Public Holding

As per the Rule No. 7.6 (iv) of the Colombo Stock Exchange, percentage of public holding as at 31st March 2017 was 10.54%, comprising 10 shareholders. (2016 - 10.87% comprising 12 shareholders)

Twenty Major Shareholders of MI As at 31st March 2017

Name	% on Total Capital	No of Shares 2017	% on Total Capital	No. of Shares 2016
1. Nilaveli Beach Hotels (Pvt) Ltd	20.94	629,580	20.83	626,240
2. A.M. Ondaatjie	15.88	477,213	15.88	477,213
3. G.G. Ondaatjie	15.88	477,213	15.88	477,213
4. T.J. Ondaatjie	15.88	477,213	15.88	477,213
5. Mercantile Fortunes (Pvt) Ltd	13.78	414,160	13.67	410,820
6. G.L.A. Ondaatjie	8.93	268,535	8.93	268,535
7. Tangerine Tours (Pvt) Ltd	6.78	203,809	6.67	200,469
8. P.R. Divitotawela and A.D. Galagoda	0.42	12,525	0.42	12,525
9. P.R. Divitotawela and R.D. Madugalle	0.42	12,525	0.42	12,525
10. N.H.V. Perera	0.33	10,020	0.33	10,020
11. J.A.S.S. Adhihetty	0.33	10,020	0.33	10,020
12. R.M.D. Abeygunawardena	0.33	10,020	0.33	10,020
13. S. Fernando	-	-	0.17	5,010
14. S. Senanayake	-	-	0.17	5,010
15. C.A. Ondaatjie	0.07	2,004	0.07	2,004
16. A.D. Rajapaksha	0.02	501	0.02	501
17. A.M. Rajapaksha	0.02	501	0.02	501
18. A.M. Dominic	0.01	151	0.01	151
19. H.W.M. Woodward	0.00	10	0.00	10
Total	100.00	3,006,000	100.00	3,006,000

Directors' Shareholdings as at 31st March 2017

Name	Position	31st March 2017		31st March 2016	
		No. of Shares held	%	No. of Shares held	%
Mr. S H J Weerasuriya	Chairman	-	0.00%	-	0.00%
Mr. G G Ondaatjie	Managing Director	477,213	15.88%	477,213	15.88%
Mr. P M Amarasekara	Deputy Managing Director	-	0.00%	-	0.00%
Ms. A M Ondaatjie	Director	477,213	15.88%	477,213	15.88%
Mr. T J Ondaatjie	Director	477,213	15.88%	477,213	15.88%
Mr. S H Jayasuriya	Director	-	0.00%	-	0.00%
Ms. P T K Navaratne	Director		0.00%	-	0.00%
Mr. N H V Perera	Director	10,020	0.33%	10,020	0.33%
Mr. S M S S Bandara	Director		0.00%	-	0.00%
Mr. P C Guhashanka	Director		0.00%	-	0.00%

Share Trading

Since obtaining listing status under the Diri-Savi Board of the Colombo Stock Exchange, share trading has been negligible.

The share trading details for the year are given below.

Name	2016/2017	2015/2016
Number of transactions	9	-
Number of shares traded	22,940	-
Value of shares traded - Rs '000	58,320	-

Management Discussion and Analysis

Relationship Capital Review

Market Value

	Highest	Lowest	Year End
	Rs.	Rs.	Rs.
2015/2016	-	-	2,500.00
2016/2017	2,580.30	2,500.00	2,580.30

Market Capitalisation as at 31st March

	Capital & Reserves	MI Market Capitalisation*	CSE Market Capitalisation	MI Market Capitalisation as a percentage of CSE Market Capitalisation
	Rs.'000	Rs.'000	Rs.'000	%
2015/2016	7,654,232	6,613,200	2,586,153,933	0.26
2016/2017	7,867,265	7,756,382	2,662,860,329	0.29

Related Party Transactions Exceeding 10% of the Equity or 5% of the Total Assets

There were no related party transactions during the year which exceeded 10% of the equity or 5% of the total assets

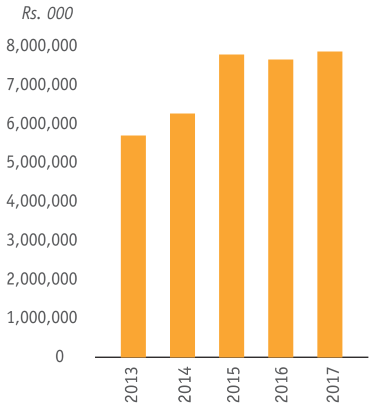
Debentures

In November 2014, the Company issued 2,000,000 senior unsecured, subordinated, redeemable four year debentures of Rs. 100/- each to the value of Rs. 200 Million. These debentures are also listed on the Colombo Stock Exchange for which Fitch Ratings Lanka Limited has assigned BBB- (lka) rating. The proceeds were utilised to optimise the cost of the Company's funding mix and to minimize the mismatches in funding exposure. The Company did not issue any debentures during the financial year ended 31st March 2017. The Company paid out the second annual interest payment to its debenture holders in November 2016.

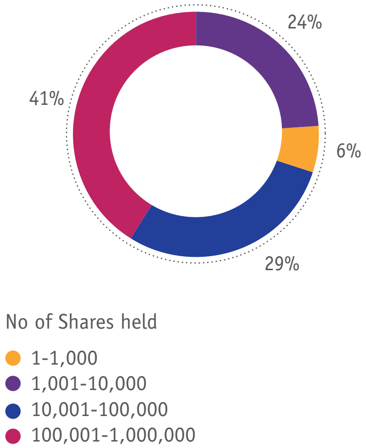
Debenture Information

	2016-2017	2015-2016
Tenure of Debenture	4 Years	4 Years
Issue date	11/7/2014	11/7/2014
Maturity Date	11/7/2018	11/7/2018
Interest Rate	Fixed	Fixed
Coupon Rate	10.50%	10.50%
Effective Annual Yield	10.50%	10.50%
Interest Rate Comparable Government Security	11.94%	11.87%
Frequency of Interest Payable	Annually	Annually
Rating	BBB- by Fitch Ratings Lanka	BBB- by Fitch Ratings Lanka
Amount (Rs. Mn)	200	200
Market Information		
Market Value - Highest (Rs)	100.67	102.62
- Lowest (Rs)	96.00	100.67
- Closed (Rs)	97.10	100.67
Current Yield (%)	10.81	10.43
Yield to Maturity (%)	10.5	10.5

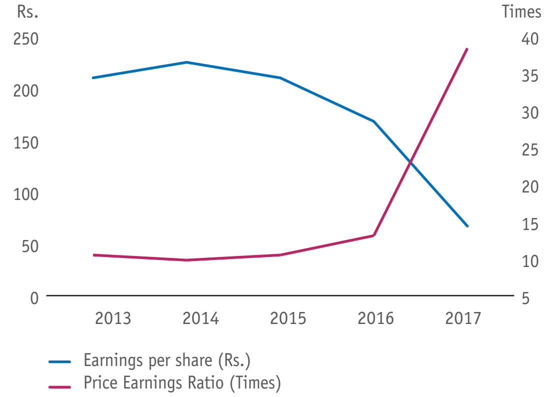
Shareholders' Fund



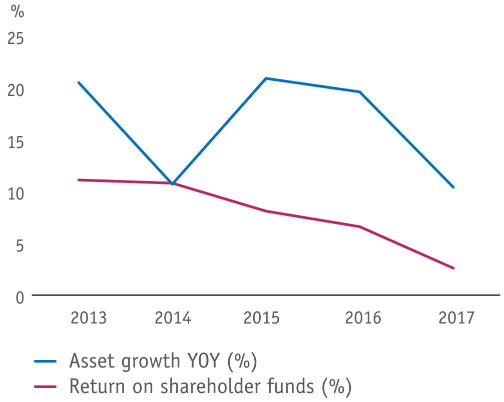
Composition of Share Ownership



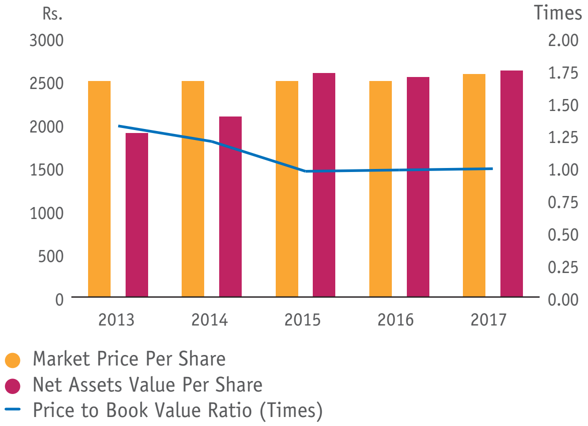
EPS & Price Earnings



Asset Growth & Return on Shareholders' Funds



Market Price/ Net Assets & Price to Book Value



Management Discussion and Analysis
Human Capital Review

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Ms. Chandima Manjusri
Employee of Mercantile Investments and Finance PLC

http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

☑ *G4-DMA*

Our Approach to Human Capital Value Building

We believe for a service organisation like ours, future success depends heavily on the way we nurture our human capital to harness a superior output. Therefore, throughout our business journey spanning fifty years, we have invested significantly in developing our workforce, to enhance their capabilities to generate the required productivity levels, whilst simultaneously keeping them satisfied and motivated. Employees remain the backbone of our operation, as they provide life to fulfil our vision and remain the most valuable asset of the Company. We have built-up a strong workforce, a team of skilled and experienced individuals who have been nurtured over the years to become financial specialists and experts in their fields. MI understands the value of human capital and has remained a caring employer, and rightfully was recognised as one of the top fifteen 'Best Companies to Work For' in Sri Lanka by the Great Place to Work Institute in 2014. MI continues to adopt employee focused human resource strategies to sustain bonding between the institution and employees, which is mutually beneficial. The Company's employee-centric approach has brought about an effective team of individuals, who remain passionate about what they do, and are positive thinkers by nature. We empower our employees to think out-of- the-box and to be creative, and provide the necessary resources including knowledge accretion that is necessary for them to excel in their fields and display talents.

We subject our workforce to a continuous value enhancement programme, that ensures both the organisation and its employees prosper and develop over time. Our human capital value building approach has been built around the solid HR policies and procedures we have put forth and it also encompasses key human resource management techniques such as manpower planning, talent acquisition, training and development and the performance measurement tools. This whole process comes under the purview of the AGM Human Resource, and reflects a transparent declaration of 'our people strategy', which is aligned to the overall business strategy.

Key Performance Indicators

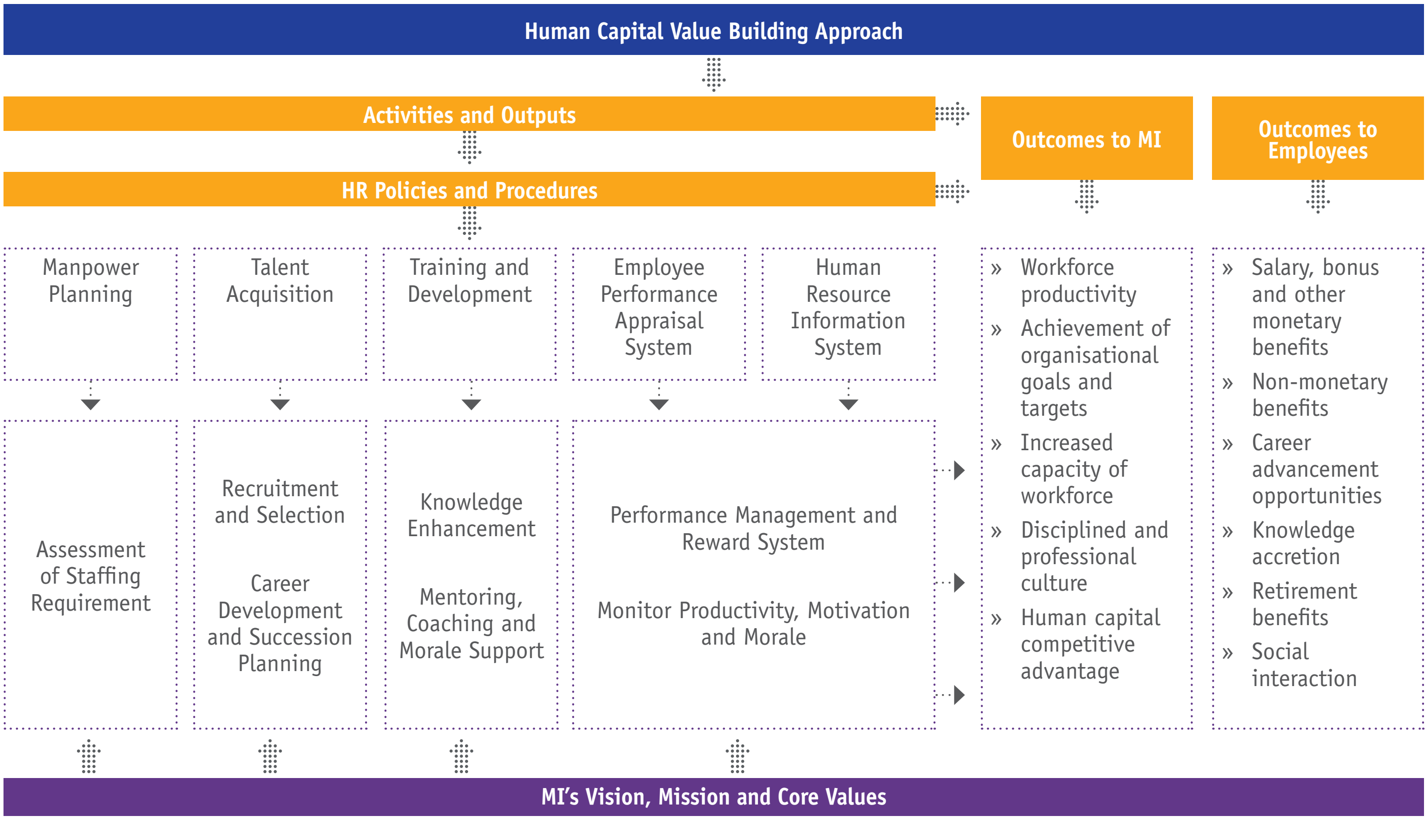
	Actual 2016/17	Actual 2015/16	% Change
Human Capital Impacts;			
Staff Strength	876	738	19%
New Employee Hires	302	264	14%
Absenteeism & Lost Days	210	413	-49%
Total Training Hours	11,070	10,526	5%
Average Training Hours per Employee	44.8	19.53	129%
Grievances Resolved (%)	86%	83%	3%

Capital Objectives

- Development of a strong productive workforce geared with skills to face the future.
- Efficient management of human resources.

Future Goals

- Completion of the fully-fledged external human resource management system by FY 2018/19.
- Average training hours per employee to be enhanced up to 60 hours.



Human Capital Value Building Approach

Activities and Outputs

HR Policies and Procedures

Manpower Planning → Assessment of Staffing Requirement

Talent Acquisition → Recruitment and Selection; Career Development and Succession Planning

Training and Development → Knowledge Enhancement; Mentoring, Coaching and Morale Support

Employee Performance Appraisal System; Human Resource Information System → Performance Management and Reward System; Monitor Productivity, Motivation and Morale

Outcomes to MI

- Workforce productivity
- Achievement of organisational goals and targets
- Increased capacity of workforce
- Disciplined and professional culture
- Human capital competitive advantage

Outcomes to Employees

- Salary, bonus and other monetary benefits
- Non-monetary benefits
- Career advancement opportunities
- Knowledge accretion
- Retirement benefits
- Social interaction

MI's Vision, Mission and Core Values

Management Discussion and Analysis

Human Capital Review

Workforce Productivity

The primary objective of our HR model is to cultivate a strong productive workforce of value that will contribute towards organisational success. In building up this required manpower base, this year we recruited 302 staff members to support the on-going expansion strategy. Nonetheless, recruitments were moderate due to the relative deceleration in branch expansion and the consolidation of the existing workforce. Greater attention this year was paid in nurturing the existing workforce which totalled 876 up by 19%, adopting a strong learning culture exercised across the Company. Through a continuous nurturing programme we developed employee skills, knowledge and capabilities, empowering them to be organisational leaders and drivers in their fields.

☑ *G4-DMA, LA11, LA16, HR12*

Human Resource Policies and Procedures

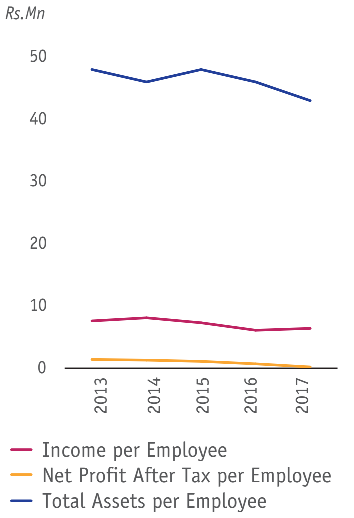
Our broad policy on human resources requires that we groom our employees professionally throughout their working lives, which will bring about perceived benefits to both the organisation and the employee. The HR policies recognise the importance of building employees' technical skills and competencies at all levels of the hierarchy and has been aligned with overall corporate objectives and goals of the Company. Policies and procedures have been designed to bring out talents and to empower employees to become financial professionals over time, paving the way for the dedicated top performers to advance in their careers. As an organisation entrusted with a high degree of responsibility, in keeping to MI's values and culture, all employees are expected to display integrity at all times and to act ethically in whatever they do. The policies further uphold equality in the workplace, giving everyone the opportunity to excel in their fields and we do not justify or condone any form of discrimination in respect of an employee's race, gender or religion. We believe that having the right HR framework and policy will certainly enrich how we manage our human capital, and accordingly the HR division was able to make necessary updates and changes to existing policy, procedures and practices, during this period.

☑ *G4-10 LA 1, LA12*

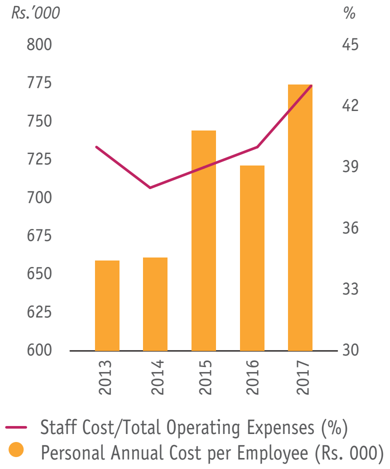
Manpower Planning

In the backdrop of the ongoing branch expansions and increased operational requirements arising from business growth, it remained vital that we planned our human resource requirements across all critical functions. Accordingly, all heads were consulted and a manpower requirement plan drawn up, and then followed up by the HR division. To fulfil growing cadre requirements, as the first option we tracked top performers from existing staff to take up these dynamic roles. When no suitable employee could be identified from within, we proceeded to a formal recruitment programme, attracting experienced and skilled individuals mostly from the finance industry. Total manpower requirements stood at 280 for the period under review, but were lower than previous years as the Company embarked on its consolidation phase in most regions. Through this two pronged strategy majority of the manpower requirements earmarked were fulfilled before the conclusion of the financial year.

Workforce Productivity



Workforce Expenditure Review



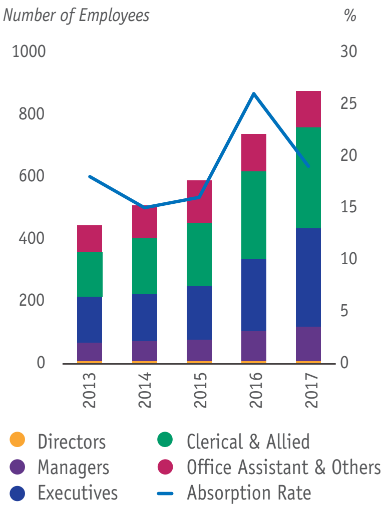
☑ G4-DMA

Workforce Composition, Diversity and Equal Opportunity

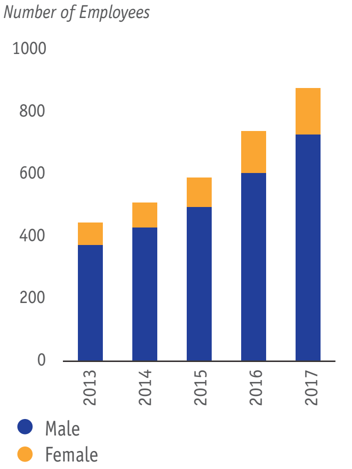
As a caring and considerate organisation, we continued to create an ideal working environment that fosters equal opportunity and adequate prospects for career progression, sans any bias towards an individual's age, gender, race, religion or creed. The remuneration policy we adopt is availed to our entire workforce without any gender bias and provides opportunity for committed performing individuals to enjoy matching rewards. From the time of recruitment, up until the employees complete their working lives, we treat all our employees with equality and discrimination is totally banned from all perspectives. 24% of our employees have remained with us for more than five years and out of this 58% have recorded service tenures exceeding ten years. This is a true reflection of MI's progressive style of people management, one that assures lasting bonds with those who dedicate their lives for the betterment of the organisation.

Our total staff strength has been increasing since inception, and we have seen a clear increase in female employees joining the organisation over time, reflected in the female gender percentage increasing by 19% on average annually over the last five years. In terms of workforce age, we are fortunate to have a well-balanced team comprising of 42% experienced employees who are over 30 years of age and a youth group that comprises of employees, most below the age of 30 years. Through a strategy of local hiring, we have identified those most fitting to work in geographically dispersed locations that we now operate in. Our ethos for diversity and inclusivity embraces employees from all religions, ethnicities and abilities.

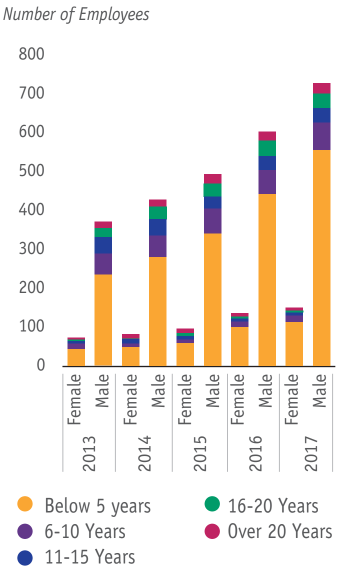
Staff Strength



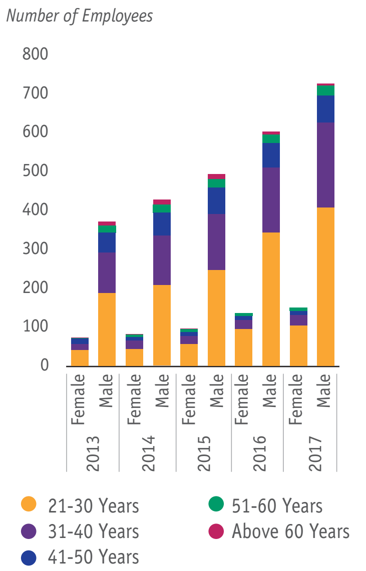
Gender Distribution of Employees



Service Analysis of Employees



Age Analysis of Employees



Province and branch-wise breakdown of human capital - Visit MI website

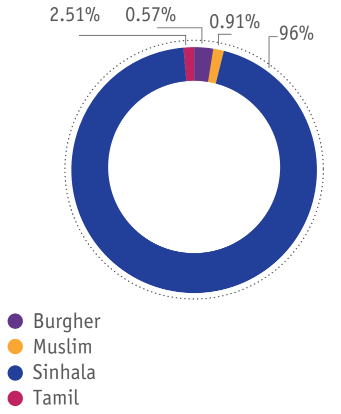
http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

Management Discussion and Analysis

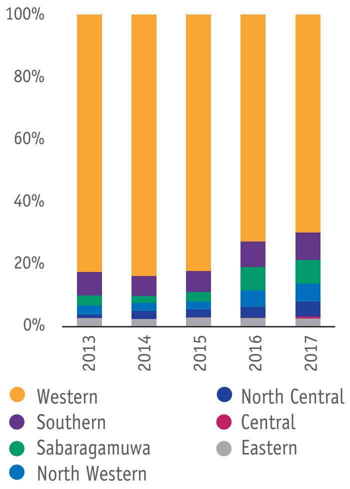
Human Capital Review

		Ethnic Group				
Gender	**Religion**	**Burgher**	**Muslim**	**Sinhala**	**Tamil**	**Grand Total**
Female	Buddhist	0	0	121	0	121
	Catholic	4	0	19	2	25
	Hindu	0	0	0	0	0
	Islam	0	2	0	0	2
	Christian	0	0	2	0	2
Female Total		**4**	**2**	**142**	**2**	**150**
Male	Buddhist	0	0	618	0	618
	Catholic	1	0	77	8	86
	Hindu	0	0	0	12	12
	Islam	0	6	0	0	6
	Christian	0	0	4	0	4
Male Total		**1**	**6**	**699**	**20**	**726**
Grand Total		**5**	**8**	**841**	**22**	**876**

Ethnic Group



Province-wise Breakdown of Human Capital



Talent Acquisition

We adopt an effective recruitment process that ensures thorough screening and selection of candidates, directed at attracting most suited and talented individuals. As a premier finance company, MI continued to be a preferred employer for job seekers wanting job security, prestige and attractive benefits, in a competitive job market. As part of the recruitment process, candidates were subject to an initial interview and then shortlisted for the final interview and selection. The applicants are assessed on their level of experience, qualifications, and aptitude for the post at hand. New recruitments reflected a 14% increase from last year, while internal promotions totalled 161, up 69% year-on-year. Our workforce comprises of 30% personnel who have been recruited from outside the Western Province, reflecting a growth of 31% in the outskirts, driven by our local hiring policy. Majority of the workforce are Sinhala Buddhists, but there is growing representation from other ethnic groups and religions. Based on the wider job scope specified for staff, formally carried out job enhancements and job enrichments were minimal during the year. Furthermore, as our business is not subject to seasonality, recruitment numbers did not vary based on seasons. (Refer table Total Number and Rates of New Employee Hires by Age Group, Gender and Region on the next page.)

☑ *G4-EC 6*

Proportion of Senior Management Hired From the Local Community at Significant Locations of Operations

As a recruitment strategy, candidates who reside within close proximity of our branches/service centres are given preference if they possess the required capabilities and experience. Close proximity from home to workplace gives the employee the opportunity to feel motivated, to devote their maximum effort when doing their day-to-day work at the workplace. Also, they are already familiar with the business environment and customer profile and will fit in faster to MI's aspirations. The cultural and traditional differences between different areas of the country that tend to be factors are not considered key concerns anymore for such employees. Based on our local hiring policies, 69% of staff have been locally hired and out of this 7% comprise senior officers locally hired.

Statistics on locally hired - visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

Total Number and Rates of New Employee Hires by Age Group, Gender and Region

Category	**FY 2016/17**				**FY 2015/16**			
	Male		**Female**		**Male**		**Female**	
	Number	**%**	**Number**	**%**	**Number**	**%**	**Number**	**%**
Eastern								
Below 30 Years	2	0.66	1	0.33	5	1.89	2	0.76
30-50 Years	2	0.66	0	0.00	0	0.00	0	0.00
Over 50 Years	0	0.00	0	0.00	0	0.00	0	0.00
Central								
Below 30 Years	2	0.66	2	0.66	0	0.00	0	0.00
30-50 Years	3	0.99	0	0.00	0	0.00	0	0.00
Over 50 Years	0	0.00	0	0.00	0	0.00	0	0.00
North Central								
Below 30 Years	17	5.63	4	1.32	10	3.79	2	0.76
30-50 Years	5	1.66	0	0.00	1	0.38	0	0.00
Over 50 Years	0	0.00	0	0.00	0	0.00	0	0.00
North Western								
Below 30 Years	21	6.95	1	0.33	18	6.82	2	0.76
30-50 Years	2	0.66	0	0.00	6	2.27	0	0.00
Over 50 Years	0	0.00	0	0.00	0	0.00	0	0.00
Sabaragamuwa								
Below 30 Years	15	4.97	1	0.33	26	9.85	3	1.14
30-50 Years	2	0.66	0	0.00	3	1.14	0	0.00
Over 50 Years	0	0.00	0	0.00	0	0.00	0	0.00
Southern								
Below 30 Years	23	7.62	5	1.66	21	7.95	1	0.38
30-50 Years	4	1.32	0	0.00	7	2.65	0	0.00
Over 50 Years	0	0.00	0	0.00	0	0.00	0	0.00
Western								
Below 30 Years	105	34.77	34	11.26	99	37.50	30	11.36
30-50 Years	29	9.60	1	0.33	20	7.58	2	0.76
Over 50 Years	18	5.96	3	0.99	6	2.27	0	0.00
Total	**250**	**82.78**	**52**	**17.22**	**222**	**84.09**	**42**	**15.91**

Employee Retention and Attrition Percentage

As a caring employer who has focused attention on the well-being of its employees, we are proud to possess a highly motivated growing workforce. We have already started to reap the benefits of investing in employee development activities, and providing the required infrastructure and morale support to them. This has led the way for the organisation to sustain high employee motivation levels, and comparatively lower staff turnover numbers recorded over the years. However, the staff turnover this period compared to total staff stood at 19% reflecting a moderate percentage increase from last year's 15%, pushed up by the nature of the finance industry and current trends. Out of the total resignations, 23% comprised female staff resignations, reflecting somewhat similar percentage resignation levels as last year. (Refer table Staff Turnover by Age Group, Gender and Region on the next page.)

☑*G4-DMA, LA9, LA10*

Training and Development

As the main driver in building employee knowledge, training and development activities played an integral role in constantly uplifting technical know-how of the workforce, equipping them with the skill sets, knowledge and experience to face the challenges and sophistication of an evolving finance industry. More importantly, by uplifting the skills of our employees, we were able to extend a superlative service to our customers, and gain the required competitive advantage across all our locations. The human resources department made sure that a comprehensive training programme was structured and implemented effectively, to eliminate the key training gaps identified in the divisions. Through these efforts, total employees subject to training was increased by 125 compared to a year before. On top of this, as a result of the initiated extensive training programmes, the total training hours per employee increased by 129% to 45 hours per employee per annum.

In-house training programmes were arranged at MI's Cotta Road Training Centre and in combination the staff was sent on external training programmes which covered technical and industry specific subjects, and regulatory changes. In addition, new recruits followed the standard induction training programme, and thereafter underwent a hands-on training phase, learning and improving their skills on-the-job. Separately, employees leading challenging functions and those

Management Discussion and Analysis

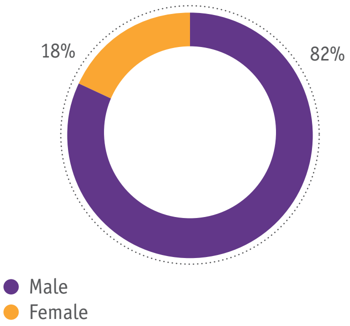
Human Capital Review

Staff Turnover by Age Group, Gender and Region

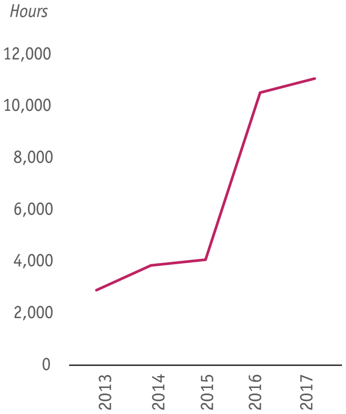
Category	**FY 2016/17**				**FY 2015/16**			
	Male		**Female**		**Male**		**Female**	
	Number	**%**	**Number**	**%**	**Number**	**%**	**Number**	**%**
Eastern								
Below 30 Years	4	2.40	0	0	2	1.75	0	0
30-50 Years	0	0	0	0	4	3.51	1	0.88
Over 50 Years	0	0	0	0	0	0	0	0
North Central								
Below 30 Years	5	3.00	4	2.40	3	2.63	1	0.88
30-50 Years	0	0	0	0	0	0	0	0
Over 50 Years	0	0	0	0	0	0	0	0
North Western								
Below 30 Years	11	6.70	0	0	2	1.75	0	0
30-50 Years	1	0.60	0	0	1	0.88	0	0
Over 50 Years	0	0	0	0	0	0	0	0
Sabaragamuwa								
Below 30 Years	5	3.00	3	1.80	4	3.51	1	0.88
30-50 Years	1	0.60	0	0	0	0	0	0
Over 50 Years	0	0	0	0	0	0	0	0
Southern								
Below 30 Years	7	4.30	2	1.20	8	7.02	2	1.75
30-50 Years	5	3.00	1	0.60	2	1.75	0	0
Over 50 Years	0	0	0	0	0	0	0	0
Western								
Below 30 Years	54	32.90	25	15.20	32	28.07	20	17.54
30-50 Years	16	9.80	1	0.60	12	10.53	4	3.51
Over 50 Years	18	11.00	1	0.60	13	11.40	2	1.75
Total	**127**	**77.44**	**37**	**22.56**	**83**	**72.81**	**31**	**27.19**

Training conducted at MI Cotta Road Training Centre

Training by Gender



Hours of Training



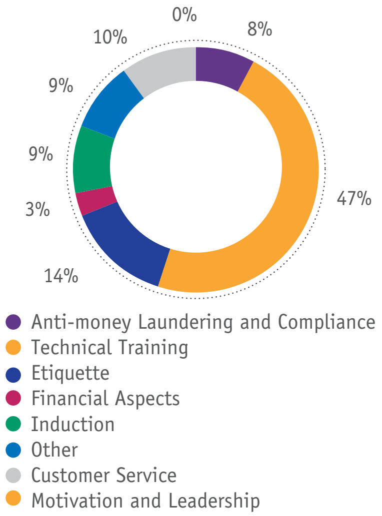
needing guidance were mentored, coached and given the required moral support.

A healthy learning culture was adopted across all layers of the organisation which facilitated continuous learning opportunities for all working within, to obtain necessary technical knowledge, and to enhance soft skills abilities such as effective communication and writing skills. By fostering this creative learning culture, employees continued to be encouraged to be innovative thinkers. This also paved the way for the creation of potential leaders from our existing workforce. Already, employees who have excelled in their fields, devoting their lives for the betterment of the Company, through their unwavering dedication and perseverance, have gone on to take up leadership roles within the organisation.

Training Conducted In-House on Anti-Money Laundering Legislation

Grade	**FY 2016/17**	**FY 2015/16**	**FY2014/15**	**FY2013/14**	**FY2012/13**
Managers and above	50	28	16	11	14
Executives/Assistants	75	183	89	61	52
Total	125	211	105	72	66

Training Programmes



Training Calender - Visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

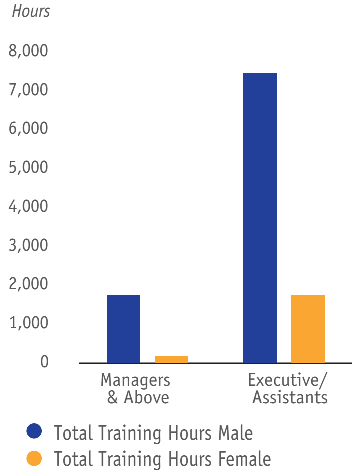
Programmes for Skills Management and Lifelong Learning

Our employees underwent extensive training and development programmes, which involves personal grooming and a life long value accretion training support, that facilitates a 360-degree understanding of work, essential to widen their skills and for capacity building.

Lifelong learning programmes covered - Visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

Training Hours by Employee Category



Appraising Performance

We conducted formal bi-annual performance appraisals across all SBU's/departments, to monitor staff performance against key goals and to reward top performers. These performance measurement tools and criteria enabled us to decide on bonuses, salary increments and additional training requirements. It also provided insight to management on consistently performing high achievers, to decide on future career advancements. A direct scorecard system was adopted for all front line staff mostly those attached to lending, deposit mobilisation and recovery divisions, that compared each employees actual performance against pre-defined KPI's. Support divisional staff performance was evaluated on more qualitative performance indicators, which assessed the effectiveness of their routine work duties combined with pre-defined additional job goals set at the commencement of a period. The individual scores generated from these two evaluation approaches enabled management to rank their staff periodically, which helped identify top performers and those performing below expectations.

Management Information on Human Resources

We continued to utilise our Human Resource Management System (HRIS) to generate a constant stream of invaluable employee information, to better manage our workforce and to take appropriate decisions. As key enhancements to the system, we were successful in implementing a fully-fledged on-line leave approval system commencing 2017 and are also on the verge of systemising the overtime computations utilising the existing thumb print attendance system. As a bold progressive step, we have made plans to acquire a renowned external HRIS system to better manage human resources. The system would be implemented during the next financial year.

Employees receiving regular performance appraising and career development in FY 2016/17

Employee Category	No. of Staff Evaluated		No. of Staff Not Evaluated	% Appraised
	Male	Female		
Corporate Management	76	8	33	71.79
Executive Officers	122	33	9	94.51
Junior Executive	126	27	10	93.87
Assistants & Allied Grades	204	75	153	64.58
	528	143	205	76.60

Management Discussion and Analysis

Human Capital Review

☑*G4-LA3, DMA (Includes sector specific DMA), LA5, LA6, LA 7, LA 8*

Employee Work Environment

A safe and conducive work environment is maintained, for the productivity, safety and convenience of all staff. We adhere to the required safety standards and continued to provide staff efficient work floor structures that include individual work stations that are equipped with necessary PC systems and other corporate equipment. During the financial period, additional floor space was provided to departments attached to Head Office premises to expand mainly the deposits, insurance, and audit divisions. We also commenced constructing a spacious lunch room for the staff members attached to the Head Office which will be concluded by mid-2017.

In terms of employee health and safety, necessary precautionary measures were taken to protect employees from physical hazards such as fire. The Company's security requirements have been outsourced to an expert security company which provides security personnel to handle security at Head Office premises. While carrying out continuous patrolling on a daily basis, they are also equipped with CCTV to monitor physical activity at all MI locations, for the safety of all our workers. Being a service oriented organisation that deals primarily in financial transactions, the type of tasks carried out by our employees do not directly pose safety risk or disease related health hazards. Hence, there is also no necessity to establish any formal joint management-worker health and safety committees. There were no material injuries to our staff while on duty, except for few small injuries. There were only 26 lost days and 215 days of absenteeism reported, deemed immaterial. A total of 536 staff members took advantage of the health insurance scheme available covering also their families for hospitalisations.

Rate of injuries or fatalities, occupational diseases, lost days, absenteeism by region and gender

Region	**Injuries (In Number)**				**Lost Days (Based On Average Number of Days Per Employee) *246 Days**				**Type of Injuries**
	Male	**%**	**Female**	**%**	**Male**	**%**	**Female**	**%**	
Eastern	0	0	0	0	0	0	0	0	
North Central	0	0	0	0	0	0	0	0	
North Western	1	50	0	0	24	10	0	0	Leg injured (Bike Accident)
Sabaragamuwa	0	0	0	0	0	0	0	0	
Southern	0	0	0	0	0	0	0	0	
Western	1	50	0	0	2	1	0	0	Leg injured (Bike Accident)

** Average number of days per employee - 246 days*

** No fatalities reported*

Region	**FY 2016/17 Absenteeism (In Days)**			
	Male	**%**	**Female**	**%**
Eastern	10	4.66	0	0.00
North Central	2	0.93	1	0.47
North Western	8.5	3.96	0	0.00
Sabaragamuwa	1	0.47	0	0.00
Southern	7	3.26	1	0.47
Western	127	59.21	57	26.57

** Occupational diseases are not applicable as there are no risks from disease directly linked to finance business, for people at work.*

*** Report was compiled from the statistics generated by the HR department by obtaining information from various heads of divisions on an annual basis.*

**** No independent contractors have been employed.*

In keeping to the Shop and Office Employees Act No. 15 of 1954, six employees were sent on parental leave, while the return to work ratio declined to 40%, due to more women resigning after maternity.

Return to work and retention rates after parental leave, by gender

	FY 2016/17	**FY 2015/16**	**FY 2014/15**
Number of employees entitled for maternity leave	150	136	95
Number of employees who took maternity leave	6	5	2
Number of employees who returned to work after maternity leave	3*	5	2
Number of employees who returned to work after maternity leave ended who were still employed 12 months after their return to work	2	2	4
Return to work rate %	50*	100	100
Retention rate %	40	100	75

** Three employees are on maternity leave and their returning dates are 11/04/2017, 18/07/2017 & 09/08/2017*

*** As a general policy, only maternity leave for females are granted as parental leave.*

**** Based on previous year's retention information.*

☑ *G4-56, LA 16*

Remedying Employee Grievances

We adopt a people-centric culture across all our divisions which facilitate interactions between all employees. The "open door" corporate culture we operate facilitates free flow of information and importantly allows staff grievances to be picked up early and to be resolved then and there by the senior management. Employee grievances are generally picked up directly by the respective heads of divisions or line management and resolved jointly with the assistance of the human resource department. Grievances that cannot be resolved or any unresolved concerns brought formerly to the attention of the HR division is firstly routed upward to the respective senior management and if still unresolved finally to the Managing Director for a solution. Any matters concerning human rights of employees and of outside parties, will be channelled upward by respective divisions to the human resources department who will consult with the top management and take steps towards resolution. The human resource division is equipped with persons of the relevant expertise and experience to deal with employee grievances of significance, be they work or human rights related. There were no reported violations against human rights which were channelled formally to the human resource division during the period.

The Board and the management require all employees to act diligently, executing their duties at all times with integrity while continuing to adhere to organisational rules and regulations. To eliminate possible grievances arising due to misunderstandings of internal rules and regulations, a "Human Resource Handbook" has been issued to all staff which specifies standard practices and rules for employees to follow including requirements on employee conduct.

Grievance formally reported and resolved

	FY 2016/17	FY 2015/16	FY 2014/15
Total number of grievances formally reported	7	6	4
Number of grievances addressed	7	6	4
Number of grievances resolved	6	5	4
Number of grievances unresolved	1	1	0

☑ *G4-EC5,LA2, DMA, LA13*

Employee Remuneration, Benefits and Welfare

The minimum salary paid to employees at MI is above the minimum statutory requirement in Sri Lanka. In accordance with the National Minimum Wage of Workers Act No. 03 of 2016, the minimum wage is Rs. 10,000 for any industry or service sector, whereas, entry level of MI is set at Rs. 14,000, and does not vary with the location of operations or gender. Location of operation is referred to as the branches and service centres, where MI carries out its business operations. Ratio of standard entry level wage to local minimum wage at MI is 140%.

All our permanent employees are entitled to an attractive remuneration package, coupled with other monetary and non-monetary benefits after making due tax deductions to comply with existing tax regulations. In accordance with labour regulations, we also contribute monthly to the Employee Provident Fund and Employee Trust Fund, while employees are also entitled to gratuity in accordance with the Payment of Gratuity Act. Apart from the annual salary increments that take place based on respective employee performance and market factors that are taken into consideration, they are also entitled to a bi-annual bonus paid twice a year. Permanent employees of executive grades and above under special considerations are also entitled to staff loans at concessionary rates.

As part of staff welfare privileges, employees in case of an emergency, could obtain temporary distress loans under special recommendations, and also seek assistance from the MI welfare association if in need of financial support. Health insurance cover is also provided to our permanent employees of executive grade and above, to their spouses and children. In addition to this medical related support, commencing from last year, all assistant managers and above are availed of a comprehensive annual medical check-up scheme at the Company's expense. Gym membership is also availed for the members of the senior management at an exclusive gymnasium located in Colombo.

From a social angle, in keeping to MI's unique culture and close employee bonding, corporate-socio events are held annually that range from departmental outings to get-togethers at external locations, which finally culminate in a company-wide annual party held during the Christmas festive season. Apart from these gatherings, the corporate sports meet, Christmas carols and other special events continue to build fellowship among employees. As an organisation built on the capabilities of our employees, as a practice the Company takes pride in recognising long standing employees and also those who retired during the year. (Refer table on Permanent Employee Benefits on the next page)

Salary Levels and Gender Comparison

Salary comparisons based on gender and also on highest paid individuals compared against average salary levels at each MI location did not reflect material deviations.

Management Discussion and Analysis

Human Capital Review

Permanent Employee Benefits

Key Benefits	**2016/17** **Rs.'000**	**2015/16** **Rs.'000**
Salaries, Wages & Bonus	551,747	419,724
Overtime	13,761	14,257
Allowance	77,582	55,812
Medical Expenditure	1,188	2,718
Health Insurance	11,860	10,801
Professional Development	1,624	1,732
Staff Loan	23,110	28,566
Gratuity	28,327	23,456
Parental Leave	506	909
Welfare Costs	1,068	1,060

☑*G4-54 & 55*

Ratio of Annual total compensation - Visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

Salary scale of permanent employees category-wise and by locations - Visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/human-capital/

Corporate Events held in 2016/17

Annual Get-together

The much awaited annual get-together of MI staff was held in grand style at the Waters Edge on 10th December 2016, with the participation of the Managing Director, Executive Directors and members of the Corporate Management. The event featured live music and other fellowship events including dancing competitions, followed up by a gala dinner.

Christmas Carols

For the fourth consecutive year, Christmas Carols were sung by the MI employee choir, under the patronage of the Managing Director, Gerard Ondaatjie. The heart-warming event was held on 16th December 2016 at the Head Office premises, to herald in the Christmas feeling once again. To make the event more meaningful and lively, children of some staff members participated in a drama, reliving the nativity of Jesus Christ.

Mercantile Cricket

MI's cricket team took part in the Mercantile Cricket E Division tournament held in 2017, making a tremendous impact, beating a number of companies to reach the semi-finals.

☑*G4-11, DMA, LA4, LA8*

Employer–Employee Relationship

The close cordial employer-employee relationship maintained over the years, continued with no concerns or disruptions for either party. Material concerns, recommendations and grievances raised through formal channels were evaluated and followed up by Management. No Trade Union functions within the Company and no collective bargaining agreements are effected by the Company with its employees. Further, no formal agreements prevail between the organisation and its employees on matters of health and safety. At the time of joining, all employees are bound to sign and accept the letter of appointment acknowledging the terms and conditions of his/her employment. A formal job description is issued to all staff upon joining, specifying the job role and responsibilities, thus eliminating any future misunderstandings. Management

MI get-together at Waters-Edge 2016

MI choir of 2016

Victorious MI Cricket team 2016/17

has the discretion to make any required material operational changes to staff job functions, but if it were to happen, usually such matters are discussed with the relevant staff member prior to implementation. No minimum notice period is required to be specified to the relevant employee, if any such changes are deemed necessary.

Human Rights Considerations

The Company respects rights of people and ensures it keeps within the standard human rights norms when dealing with employees and external parties. MI's organisational policies, procedures and practices have been developed in a manner that it does not contravene such key human rights considerations. Similarly, MI's corporate principles and value system highlight the importance of respecting the human element and the need to safeguard human ideals. Whenever the Company embarks on any new strategy and material operational changes, we ensure human rights considerations of our workforce and external parties are safeguarded and we avoid proceeding with matters deemed in contravention of any known human rights principles. All five branches opened this year for the purpose of increasing the scale in terms of reach was done without impacting any known human rights concerns. There were no human rights violations or material impacts reported formally to the human resource department during the year.

Our Policy on Human Rights

In keeping to our principles and value system we continued to inculcate a learning work environment and a profound culture that holds no boundaries when it comes to career development and progression. Employees of either gender are given equal opportunity to display skills and to excel in their fields. As a strict human rights policy, we ensure our current workforce and future recruitments do not involve obtaining services of individuals below the specified legal age for employment, for any requirements whatsoever. The Company sustains healthy acceptable working conditions to all employees by keeping to accepted health and safety standards. Our human resource policies uphold best in the industry HR practices to manage employees, to derive perceived productivity levels. It conforms to prevailing labour regulations. The human resource division continued to act as the guardian of these requisites, to ensure that the policies are effectively practiced and complied with.

☑ *G4-DMA, HR1, HR2, HR9*

Human Rights Assessments

No part of MI's operations including any investment agreements, were directly subject to human rights screening, impact studies or assessments during this period. No separate human rights clauses were developed and incorporated into agreements this period. No separate training was also conducted on human rights policies practiced at MI. Nevertheless, the Company continued to give due attention to key human rights considerations before proceeding with any major operational plans that include establishment of new business locations. Through the "open door policy" and formal reporting mechanisms, management gathered the required intelligence from various operational sources to assess whether any employee, customer or community was subject to human rights violations.

☑ *G4-DMA, HR7, HR 12*

Security Personnel Training

As part of the duties of the trained security officers deployed by the external security firm, employee safety related rights and also those of outsiders coming into the Head Office premises were safeguarded appropriately. Security personnel upholding best-in-class security practices and norms are well equipped to handle security situations including security breaches. Security personnel have the right attitude to deal with people in a humane manner and to handle security situations effectively. Apart from basic hands-on training given, no separate human rights training was afforded to security personnel stationed at MI, during the year.

☑ *G4-DMA, HR3*

Equality for all at the Workplace

The Company does not discriminate against any individual based on their age, gender, religion or race for any reason and expect parties that transact with us also to uphold similar values. There were no incidents of discrimination reported through our formal channels during this period.

☑ *G4-DMA, HR5, HR6*

Total Prohibition of Child Labour and Forced/Compulsory Labour

We ensure that our recruitment policies conform to prevailing labour laws that require strict compliance to the minimum age limit for providing employment. No individual is subject to forced labour or has been engaged against his/her free will at any of our locations. MI's human resource policies completely prohibit enforcing of child labour and young workers exposed to hazardous work, in any of our operations. No part of our operation involves any form of forced or compulsory labour. Employee management is conducted by complying to laws and regulations relating to employee working hours, payroll processing and other key HR requisites, in-line with the Shop and Office Employees Act No. 15 of 1954 as amended, and the Wages Boards Ordinance. Currently, we are not in a position to evaluate labour policies of our suppliers as our dealings with them are minimal. However, if any supplier becomes material to us in future, we hope to evaluate their labour policies accordingly.

Management Discussion and Analysis
Intellectual Capital Review

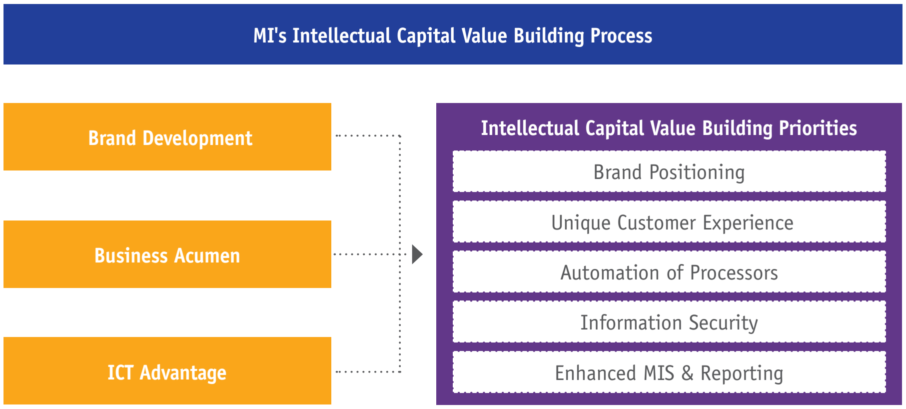
> "Some organisations have embraced digitisation whilst others seem to operate in a technology and process backwater which may have been considered modern in the past decades.
> At MI I have witnessed a clear intent by the Management to continuously modernise business processes in keeping with the most recent developments in ICT. I am confident that MI is well geared to face future complexities and sophistication".

Lasith Nanayakkara
IT Consultant

http://mi.com.lk/value-creation/value-creating-six-capitals/intellectual-capital/

Our Approach to Creating Intellectual Capital

As one of the oldest finance companies in Sri Lanka, our expertise in the industry dates back to the sixties in the area of vehicle financing. The know-how and business intelligence we continue to accumulate coupled with strong brand that we possess and whose value increases each year, equally supported by the advanced technology we embrace particularly to operate our ICT systems has enriched our intangible assets base, to what it is currently. To differentiate ourselves from others, in an increasingly competitive financial market, it is vital that we keep building the right business intelligence and know-how, to stay ahead. We are of the view that the evolution that is happening within the financial markets, is due to two factors. Increased competition and market saturation has led to the industry looking for more innovative ways of doing business, through differentiation which offers customers a value proposition and not just solutions. The other key factor has been the rapid advancement in technology, particularly the use of Information Communication Technology (ICT)/digitisation to support users in striving for service excellence and competitive advantage. Taking note of these factors, our strategy has been to make full use of our know-how and capabilities built up over the years, and also embrace digitisation particularly as a tool to gain competitive advantage. In furthering the creation of intangible value, we strive to position ourselves as a trusted financial services provider for over five decades, emphasising on the impeccable track record we have gained and the financial solidity of the MI brand.



Key Performance Indicators

	Actual 2016/17	Actual 2015/16	% Change
Branding Impact :			
Amount Spent on Branding/Awareness Building (Rs. Million)	60	85	-29%
Market Share (%)	2.91	2.66	9%
Business Intelligence:			
Know-how in Vehicle Financing (In years)	53	52	2%
Human Capital Intelligence (Average Years per Employee)	7.32	7.68	-5%
Information Communication Technology :			
Actual/Planned Investment in ICT (Rs Million)	274	0	100%
ICT Manpower (In number)	12	11	9%
ICT Related User Training (In hours)	5,145	2,381	116%

Intellectual Capital Milestones in 2016/17

- Expanded the network, awareness creation and brand building, utilising a communication and visibility driven strategy with 360-degree attack from all fronts.
- Absorbed ten skilled new recruits, who had already gained more than five years' experience in the finance field.
- A world renowned total computer solution that specially caters to the needs of the financial services sector has been selected.
- Won two coveted annual report awards from two recognised local accounting bodies and four international awards endorsing MI's commitment towards transparent reporting, good governance and sustainable standards.
- Launch of new corporate website commencing 2017, which allows our stakeholders to obtain a wide array of corporate information and current news.
- External expert brought in to review the use of the SLIPS system, microfinancing process, and embracing suggested best practices.

Capital Objectives

- Acquiring business intelligence to remain at the forefront in the marketplace.
- Enhancing top of mind recall of customers.
- Technology support for competitive advantage.

Future Goals

- Increase market share from 2.91% to 4%.
- Completion of the full migration to new external core business system before 31st March 2018.

Management Discussion and Analysis

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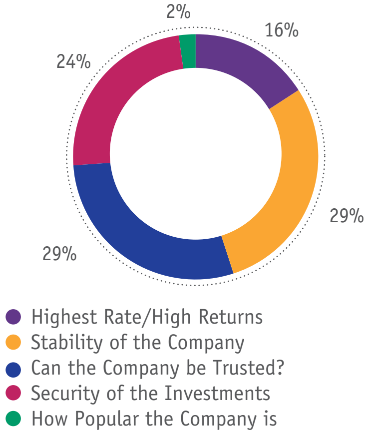
Brand Development

We have cultivated our brand "MI" over the Company's long history, as a vibrant customer-friendly dependable name in the non-banking and financial services sector. The brand identity we continue to portray justly highlights MI's image as a prudent but aggressive organisation, while being renowned to be a caring, friendly specialist in the field of financing. We promote most of our products under the "MI" logo and that makes it easier for us to market the wide array of products we possess, as it has "top-of-mind recall" in the minds of our existing customers and prospective customers. Branding which forms part of our marketing communications plan, comes under the direct purview of the Senior Manager branding and communications, who reports to the director credit and marketing and has a dotted line relationship with other business divisional heads. We use both above-the-line communication plus below-the-line activity for brand positioning and brand building, to fortify "top-of-mind recall", among people from a wide array of communities we now cater to. The perceived value of our brand keeps growing with every successful step we take, and is further fortified from the feedback received from the customer survey carried out for this financial year.

Brand Attractiveness Factors -MI



Business Acumen

We possess an experienced workforce that continues to accumulate a wealth of knowledge, expertise and wisdom on the job and through the daily exposure gained by working for a reputed pioneer in the non-banking and financial services sector. We are proud to observe that 14% of our workforce has been with us for more than ten years, while 4% of our staff has been in the finance industry for over twenty years. We have gathered a strong network of agents, who possess the required links to potential business avenues as well as contacts with vehicle sales businesses around the country, and they provide a wealth of invaluable information to us, to better future prospects. During our journey of fifty years, we have also developed a strong customer database, and other vital business information about profiles of people, markets, geographic dispositioning etc. Moreover, the wealth of knowledge and acumen gained in relation to the motor vehicle market which includes sound understanding of people's expectations on vehicle financing, ability to accurately estimate security valuations and other industry acumen has been key to our ongoing success. Based on our strategy and target estimates, we hope to further strengthen our workforce during 2017 by recruiting experienced personnel to lead some of the planned activities in the years ahead. This is in addition to recruiting more than 65 experienced individuals from within the finance industry, within the last three years.

Finance Field Experience Grade-Wise

Grade	Five years and above experience in the finance field (Number of employees)
Senior Management	6
Manager	29
Executive	55
Clerical	14

Information Communication Technology (ICT) Advantage

As another strategic tool in gaining competitive advantage, we ensured our ICT framework and infrastructure is kept top notch, taking bold measures to enhance ICT capabilities significantly going forward. Firstly, we made plans to acquire a renowned external advanced ICT platform to be implemented before the end of the next financial year. Based on the guidance of an ICT consultant, taking a long term view we carried out an AS IS study of the existing system to establish existing system gaps in meeting future ICT requirements of the Company. After evaluating a number of suitable systems available in the market, we eventually selected an effective system from an internationally renowned vendor. While this migration will happen within the next twelve months, we made necessary changes/ modification to the existing in-house built ICT system to improve and enhance its capabilities, to face the growing dynamism in the finance industry. The ICT platform adopted therefore, remained very effective, and encompassed an all-inclusive system with the necessary features to assist users in extending a speedy professional service to our customers. Similarly, ICT was used as the main vessel to facilitate the accumulation, collaboration and dissemination of vast amount of key management information and business intelligence, to make quality decisions, and also to expedite regulatory reporting responsibilities. Through a versatile technology savvy team of IT experts, a number of significant system enhancements and system upgrades were initiated, to make the existing system more user-friendly, agile and scalable to meet the growing demands of the business. At the commencement of the year, we revisited the ICT framework and system structure and with the advice of the consultant were able to make the requisite changes to enhance system configurations, strengthening capacity as well as system security. During this review process, key ICT processes, practices and procedures were also reviewed and further fine-tuned to ensure that they conform effectively to the requirements of the ICT policy framework which includes the information security policy put forth by the Board.

Key ICT Strategic Priorities

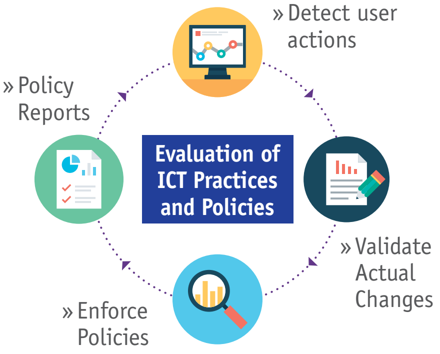
- Enhance ICT capabilities to deliver a superlative customer service
- Widening management information via ICT to make pertinent decisions
- Safeguarding data from intruders

Key ICT Steps Undertaken in 2016/17

- Significant system enhancements made to existing systems to widen its capabilities and safety
- Acquiring a renowned external human resource management system, to be implemented in 2017/18
- Making capital investments and other resource commitments to embrace an advanced external ICT system
- IT consultant support to in-house ICT team
- Structured ICT user training and round-the-clock user support

ICT Standards, Policies and Procedures

The Board of MI recognising the importance of digitisation, demonstrated strong oversight over ICT related activities, and emphasised the need to adhere to industry accepted ICT standards and protocol. Accordingly, the ICT division and all users are expected to follow the standard ICT policies, practices and processes which have been formally put-forth via the ICT Procedure Manual (IPM), Information System Security Policy (ISSP), System Development Standards (SDS) and the ICT Contingency Plans developed. Through a professional approach, these policies are directed at maximising perceived benefits from the system, ensuring its safety, soundness and credibility.



The development of ICT policy and procedures remain an on-going process and operates as a cycle where we monitor user actions and thereafter validate actual changes in order to ensure the effectiveness of the existing ICT policies, practices and procedures. Additional policies that are developed to bridge any gaps are reported back to the end users, so that there is widespread communication of ongoing organisational ICT expectations for all to know and follow.

Compliance audits on our ICT system and sub-systems are conducted with the support of Messrs Ernst and Young Chartered Accountants, system audit team while both the external auditors and the internal audit divisions are required to review general ICT controls when they cover their standard audit programmes on an on-going basis. Any non-compliance against the ICT policy, procedures and contingency plans were reported back to the Audit Committee for their immediate attention and resolution. Our ICT systems conformed to the standard requirements of the Sri Lanka Accounting Standards and also to the Central Bank rules and guidelines. Licensed software was continued to be used in the operations of the Company, in compliance with the Sri Lankan Intellectual Property Act No. 36 of 2003.

Managing the ICT Elements

We adopt a comprehensive ICT framework that covers all the necessary key ICT elements associated with a world-class system, giving its users advanced system features with online system connectivity and access to the database from both the Head Office and from all regions that we now operate in. The core system is internally

Management Discussion and Analysis

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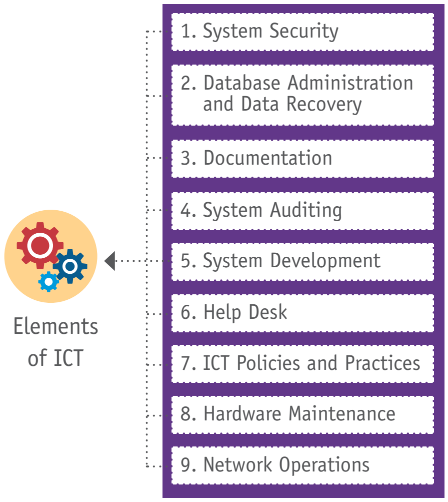
developed and uses IP-VPN technology through a renowned ISP provider in Sri Lanka. The ICT systems support all levels of the Company's hierarchy, giving more than 800 users access, thus facilitating timely and effective decision making on a daily basis. Our ICT framework comprises of nine core elements that are interlinked and administered centrally by the ICT division.

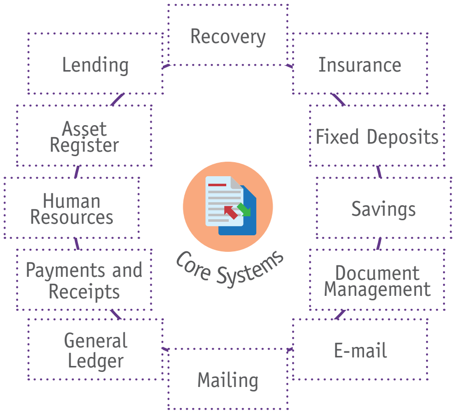


The AGM- IT heads the in-house ICT division which comprise a total of 11 staff members, who are experienced in handling all hardware requirements, systems development and configurations, network operations, system security and database administrations as part of their routine duties. During the year, a fully-fledged IT help desk was established with a hotline number for all users to lodge ICT associated issues. With the support of a dedicated ICT mobile team, such user complaints were reviewed and resolved at user locations in a speedy manner minimising the down-time and work disruptions.

ICT's Role in Simplifying Operations and Driving Efficiency

We possess a unique information technology system that has evolved over the years to become a highly reliable and stable multi-user client server, in keeping pace with the computer related technological advancements and needs of the industry. In executing core operational functions of the Company, a stable and reliable platform has been established through a world renowned Oracle Database Management System. The network servers run on Microsoft Windows Server 2008/2012, while both mail and proxy servers run on Linux. In order to speed up data processing, MI's software modules uses ".NET" platform which enhances compatibility with new operating systems and hardware solutions. MI's core system supports all key front-end and back-end operational business functions, which are fully automated. The systemised front-office functions include our total lending operation, recovery operation, fixed deposits, savings and insurance while back-office functions such as payments, receipting, inventory management and the general ledger are also fully automated.

As a key highlight this year, ICT played a huge part in assisting the ongoing decentralisation of specific operational processes. Through unique ICT solutions, we were able to automate most of the decentralised manual operations adopted recently. With the hope of decentralising the full deposit operation, plans were also drawn up for the proposed new system to provide additional system support, particularly to expedite the issue of deposit certificates directly at branches. Apart from these specific modifications, user features associated with the core system and its sub-systems were further enhanced to mainly increase user-friendliness and widen user options.



With the guidance of the IT Consultant, technical advice was sought to improve systems configurations, its reliability, efficiency and effectiveness. With the consultant's support, radical system changes were also introduced to improve overall ICT architecture, to safeguard the database from intrusions, etc.

New Technological Developments

» Migration to a Core Banking System

We commenced negotiations with an international core banking software provider to provide us with a widely equipped computer system that embraces the required system capabilities to move into the future, even to cater to needs beyond this decade. Through the support of an external consultant, we analysed our future ICT requirements, and took this bold decision to migrate to a renowned ICT software system, enhancing MI's ICT capabilities from the existing in-house developed system with the long term in view. The implementation process is planned to be concluded by financial year 2017/18. The software provider will provide all core business functions and this will mainly encompass loans, deposits, recoveries, customer care, finance and support functions. With the introduction of the new system, state-of-the-art hardware will be configured to increase capacity and the number of user friendly features in the system.

» Corporate Website Launch

The Company launched its new corporate website www.mi.com.lk commencing in January 2017, a vibrant power packed site, far more informative than its predecessor. All our stakeholders can obtain a wide array of corporate information from the website, developed using expertise of an external web developer. The site houses information about the Board and management, products and services, investor information such as the latest financial results, on-going sustainability initiatives and current corporate achievements and other pertinent informative matters relevant to the public and stakeholders.

» Broad-Based ICT User Reports

By significantly increasing the number of reports, a wide array of management information was supplied to all users through the ICT system. This helped management in closely tracking performance from various perspectives and to take appropriate decisions in a timely manner. The in-house software development team was responsible for the development of a number of new user reports for the period under review.

New key ICT users reports - Visit MI website

http://mi.com.lk/value-creation/value-creating-six-capitals/intellectual-capital/

Managing ICT Risk

In an increasingly dependent ICT environment, ICT risk management played a vital role in managing associated risk, especially considering the importance of systems for the day-to-day running of operations and also the need for data security. Based on ICT systems compliance reviews and observations stemming from the audit, we were able to tighten system controls, increasing the number of standard checks and balances embedded within the system, and strengthen security features to protect data. We also evaluated the Company's readiness to respond to any unforeseen contingency events, by revisiting ICT contingency planning actions and making due changes with the help of the ICT consultant. We continued to adopt best ICT risk control practices which helped us eliminate disruptions to ICT systems by way of a Disaster Recovery Plan, increase system security features, and to protect authenticity of the large amounts of data held within our databases.

Listed below are some of the key contingency measures undertaken to manage system related risks, mostly to protect data, its accuracy and to eliminate unauthorised access:

- Central file servers, database servers and automated data replication servers were kept fully operational to replicate data to the special Disaster Recovery (DR) sites, thereby minimising any possible data losses.
- The main systems were backed up by UPS systems and by auto starting power generators, as an additional precaution.
- Firewalls, cloud security services, Active Directory (AD) security policies, firewalls and VLAN infrastructures were implemented within the Company's network as a means of securing the ICT system from external and internal threats.
- Audit of systems with special focus on the deposit system, recently implemented SLIP system and the microfinance system was conducted with the support of a special ICT review team of Messrs Ernst and Young, Chartered Accountants. We adopted key recommendations made by the experts to improve system controls and security.

ICT Linked Training

Training was intensified among users, mostly as means of getting existing users and new users familiarised with the available options on the IT system. This helped us maximise the potential of the total system, for better performance results. Users were provided general training utilising the resource personal of the in-house ICT team while training on an ad-hoc basis was arranged whenever new system changes were installed or when requested by users. A dedicated mobile ICT team was active across the branch network, in coordination with the help desk, to assist users on troubleshooting and other related ICT support. Branch users were given assistance and hands-on training by the mobile operation staff, apart from centralised training organised in-house. The general topics included the use of key system modules, applicable user policies and procedures including duties related to the ICT security policy.

Management Discussion and Analysis
Natural Capital Review

Rotary Tree Planting Project

Mercantile Investments joining the 'One Million trees' planting project this year with other corporates is certainly encouraging, and would support the building of a greener environment, that is healthy and sustainable to all living things.

Dion Schoorman
Project Director
Rotary One Million Trees Trust (Gte) Ltd

http://mi.com.lk/value-creation/value-creating-sixcapitals/natural-capital/

☑ G4-DMA

MI's Approach in Managing Natural Capital

MI as a responsible corporate citizen has embedded an environmental perspective into its core business strategy, having understood the importance of preserving and managing the natural capital. Being a financial service provider, MI is not a significant consumer of natural resources and thus the impacts to the environment from our business operations are set at a minimum level and retrospectively the impacts from the environment does not directly affect our business operations. However, irrespective of their being minimal impacts to the environment from the business, the Company in its journey towards sustainable value creation has established a Natural Capital Value Creation Process, which focuses on enhancing our green responsiveness and green habits, and seeks ways to protect the environment, by implementing policies and procedures that assist the management team in achieving the corporate goal of preserving our environment and minimising the impact of our carbon footprint and waste from our corporate endeavours, in meeting the needs of all our stakeholders.

To ensure the commitment at the corporate level to protect natural capital, we have implemented various corporate management mechanisms, such as the Sustainability Policy, Code of Conduct, Corporate Governance Codes, and Environmental Governance Policies. MI, as a responsible premier finance company has always strived to achieve a standard of compliance which exceeds the mere legal requirements by embracing global best practices for environmental governance in addition to the mandatory environmental regulations.

We always encourage both internal and external stakeholders to utilise natural resources responsibly and to minimise and compensate for the impact of their activities. MI has, also embraced strategic partnerships with 'Green Conscious Groups' and also focused on development of our green lending policy towards more environmentally friendly funding.

With the emergence of critical environmental issues resulting from depleting natural resources, effects on ozone layer, global warming and climate change, MI has paid close attention to its operations to identify ways to support the environment. This year too, in journeying towards sustainability, we have taken steps towards fostering environmental sustainability. We engaged with our employees and the society to bring merits to our natural capital through many environmental initiatives. MI is committed in managing and promoting sustainable use of natural resources in our operations. MI's exertions in managing environmental impacts have resulted in meeting varying expectations of our stakeholders, organisational sustainability in the long run and also in minimising operating costs and reputational risks.

Key Performance Indicators

For the financial year	FY 2016/17	FY 2015/16	% Change
Green Responsiveness			
Number of green training hours	25	0	N/A
Green Habits			
Materials**			
Paper Usage (reams)	7,210	6,306	14%
Paper Recycling (as a % of total consumption)	15%	17%	-2%
Energy			
Electricity Utilisation (kWh)**	619,824	667,308	-7%
Total Fuel Usage (Litres)	816,231	605,770	35%
Energy Consumed per Employee	1,919	2,132	-10%
Water**			
Total Water Usage (Units)	8,308	8,304	0%
Emission			
Total Carbon Footprint (Tonnes)*	2,447.27	577.92	323%
Environment Protection			
Monitory Value of Green Investment (Rs.)	356,750	549,900	-35%
Green Corporate Policy			
Green Lending Portfolio (Rs. Mn)	1,517	859	77%

* *Extended the carbon footprint review scope from Head Office to all locations from 2016/17.*

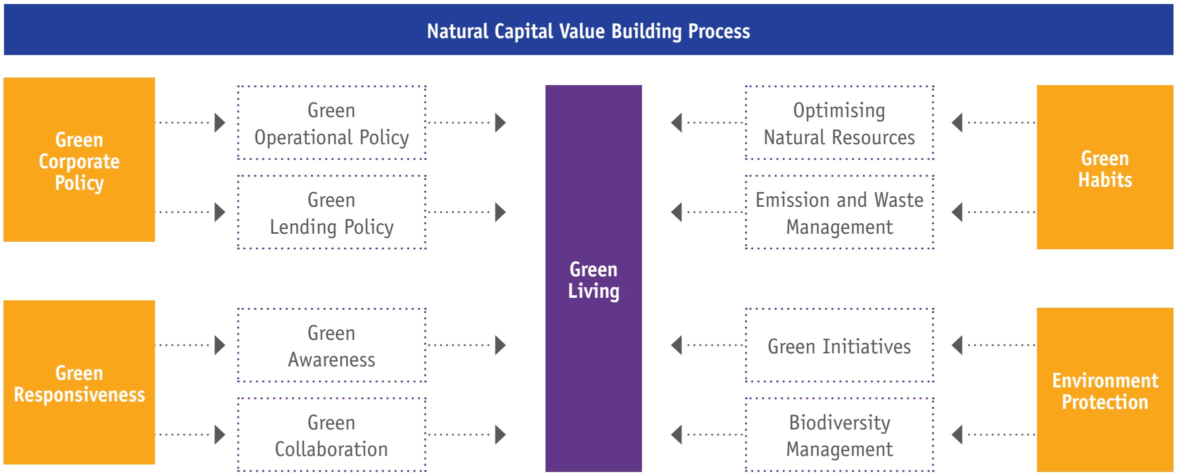
** *All Information related to head office only.*

Capital Objectives

- Reduce Carbon emission levels
- Increase the number of strategic partnership on sustainability activities to five partnerships
- Use of renewable resources

Future Goals

- Introduce a carbon management policy by 2018
- Reach carbon neutral status by 2020
- Setting up of a model solar powered service outlet by 2018



Management Discussion and Analysis

Natural Capital Review

Our Green Corporate Policy

Our green corporate policies provide a reliable framework to manage environmental concerns. These policies are aimed at the efficient use of natural resources, as well as taking measures to manage environmental impacts through prevention, mitigation and in certain instances compensate by giving back to the environment through environmental restoration efforts such as tree planting, whilst ensuring associated risk and statutory obligations are addressed. The total focus in this instance is that we do no harm to Mother Nature or the environment through our routine business operations.

Green Operational Policy

We strive to control our carbon footprint and waste, and we encourage stakeholders to operate in a similar manner to bring in value to natural capital. We have extended our diligence inculcating green practices and initiatives geared for the workplace and the community. Environmental considerations are reflected in our key corporate strategic decisions, such as when we set up a new branch or relocating an existing one. MI, as a responsible corporate citizen, ensures its business operations affect the environment to a minimal level. Further, MI encourages employee awareness and involvement in local community based environmental initiatives and understanding the importance of preserving natural capital.

☑ *G4-DMA on products and services energy requirements and environmental impacts,EN7, EN27, EN28 & FS 8*

Green Lending Policy

As a Company extending financial support for the community, our direct impact on the environment is insignificant. However, our core business of vehicle financing may have an indirect impact on the environment. Therefore, in recognition of the importance of environmental sustainability strategy, MI encourages its customers to opt for more environment friendly and energy efficient vehicles, including hybrid and electric motor vehicles. By limiting funding support for certain categories of vehicles which include the three wheeler market, our indirect impact on emission levels have been curtailed. We hope to embark on a much wider environment supportive programme by incorporating a stronger green lending policy in the future.

Understanding and managing the environmental and social risks associated with the companies with whom we work is essential to minimise the overall impact from our business operations. Therefore, we pay special attention to the purpose of our lending activities and the funding which we advance to our customers.

MI does not finance transactions relating to the following:

» Activities that would result in the degradation of protected critical natural habitats as designated

» Activities that would involve the purchase of timber from illegal logging operations

» Production or trade in any product or activity deemed illegal under host-country laws or regulations

We also believe by extending financial support to the agricultural sector which is further propelled by our interest in growing the microfinance portfolio, will reduce our indirect impact on the environment going forward.

Hybrid/Electric Lending

Environment Benefiting Products	Total Outstanding FY 2016/17 (Rs. Mn)	Total Outstanding FY 2015/16 (Rs. Mn)	Variance (Rs. Mn)
Hybrid	19,610	4,638	14,972
Electric Vehicles	154	159	(5)

☑ *G4-EC2*

Financial Implications due to Climate Change

Key Indicators	FY 2016/17	FY 2015/16	Change %
Risks from Exposure to Agriculture and Agri-Based Industries			
Agriculture and Related Lending Portfolio (Rs. 000)	901,570	854,582	5.5%
Total Agriculture Related Disbursements (Rs. 000)	546,206	655,371	-16.66%
Non-Performing Portfolio Relate to Agriculture and Related Lending (Rs. 000)	90,819	100,421	-9.56%
Non-Performing Ratio (%)	10%	11.75%	-14.28%
Environmental Initiatives			
Environmental Investment (Rs. 000)	357	550	-35.09%

Product Contribution in Building Natural Capital

Out of the product mix, our lease and microfinance business directly contribute to environmental supportive programmes, which provide the protection to wildlife of the country and also assist our clientele in safeguarding themselves from environmental hazards. By redirecting part of the revenue towards two separate funds, which totalled to Rs. 1.8 Million, the Sustainability Governance Committee plans to commence wildlife protection projects starting from FY 2017/18.

Moving ahead, we hope to develop policies to assess the environment compliance status of industrial borrowers in more detail.

Green Responsiveness

As an organisation committed in creating a greener environment, our responsiveness towards the development of natural capital during the reporting period concluded was heartening. We were able to obtain involvement of some of our staff to carry out various worthy environmental initiatives, and are in the phase of creating green awareness among our employees, by arranging briefing sessions of value.

As a result of 20 man hour training programmes,

- Microfinance staff together with their clients have cleaned a selected beach area in Ambakadawila, Chilaw and installed garbage bins.
- Customers have earned an ancillary living by selling waste, such as dried rice, compost, etc.
- Waste disposal taking a more streamlined approach.

Further, the Company conducted an awareness session relating to e-waste for branch managers. MI will implement e-waste system within the Company in coming years.

Green Collaboration

Having understood the importance of investing in green initiatives, MI collaborated with several stakeholders during the FY 2016/17, with the objective of reinforcing its green initiatives and dispersing the ultimate benefits to the environment and the society as a whole. The Rotary Club, Sri Lanka Climate Fund and Think Green (Ltd) are some of the green stakeholders we partnered with. The Company tends to create an environment friendly working background, by initiating green practices within the Company recognising the significance in individual participation and collective team work in creating a greener environment.

Similarly, MI joined hands with 'Think Green (Ltd)' to manage electronic waste. This is also a collective practice, where employees are required to dispose electronic waste in a manner that the environment or human lives are not harmed. Along with 'Think Green (Ltd)', MI also collaborated with Sri Lanka Climate Fund in FY 2016/17 to measure the extent of the negative impacts of our operations and to streamline our operational activities to reduce our carbon footprint while focusing on the activities of generating carbon credits.

Green Habits

Optimising Natural Resources

Our green habits have evolved over time to better manage the materials we use, our energy intake and our water usage. We encourage the workforce to work together, to reduce wastage and recommend practices and processes that will reduce the use of natural resources.

☑ *G4-DMA on Materials EN1,EN2*

Material Management

Controlling Consumable Intake

Considering the nature of the business, MI does not use materials to a significant extent. However, owing to the branch expansion and increased business transaction volumes, 'paper' and a few materials such as printer cartridges are used frequently. These items are made of scarce resources and hence, as a responsible corporate, MI has its recycling methods in place, in order to ensure its impact on environment is minimised. Items recycled include papers and box files. As another measure, usage of stationery and consumable items is closely monitored at department and branch level, with the introduction of the inventory management system and strengthening of the stores unit this year.

Stationery and consumables that are either reused or recycled remained a significant percentage of total usage of consumable items, as shown in the table G4-EN 1, EN 2 on next page.

Working Towards a Paperless Environment

MI invested in a Document Management System(DMS) in order to create a paperless business environment which will eventually lead to the securing of natural capital. The DMS is developed to fulfil requirements core business units to retrieve key documents and this has now been extended to support other units as well. This system has enabled the Company to reduce paper usage and avoid movement of duplicated hard copies between Head Office and branch locations. During the year, MI has further stepped forward to strengthen its online based payment modes which facilitate reduction in paper usage, while contributing to operational effectiveness.

Management Discussion and Analysis

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☑ *G4-EN1,EN2*

Recycled Item	**Items Consumed**		**Items Recycled ***		**% of Items Recycled Against Total Consumption**	
	FY 2016/17	**FY 2015/16**	**FY 2016/17**	**FY 2015/16**	**FY 2016/17**	**FY 2015/16**
Paper (Kg)	18,025	15,765	2,756	2,703	15%	17%
Box Files (Number)	1,035	992	517	450	50%	45%

* Information relates to Head office

Consumable and Stationary Usage Trend

Type of Item	**FY 2012/13**	**FY 2013/14**	**FY 2014/15**	**FY 2015/16**	**FY 2016/17**
Photocopy Paper					
- A4	2,900	3,968	4,613	5,549	6,574
- Legal	151	200	263	228	164
- A4R	335	374	421	529	472
Total (Reams)	3,386	4,542	5,297	6,306	7,210
Ink Cartridges (No. of cartridges)	387	256	267	237	212
Photocopy Toner, fax Toner & Laser Jet Printer Toners (Number)	625	897	1,116	1,771	1,924
Box Files (Number)	400	301	1,078	992	1,035

MI has emphasised the need for a sustainability driven paperless working environment, upgrading its systems to provide automated daily reporting requirements that also includes information e-mailing to users in an automated environment.

☑ *G4-DMA on Energy Consumption, EN3, EN4, EN5, EN6, DMA on transport, EN30*

Energy Management

MI's primary source of energy is electricity, which is used for day-to-day operations within the organisation. As a Company which has identified the importance of preserving scarce resources, significant measures were adopted by MI to minimise the usage of electricity. Moreover, numerous actions have taken place in order to optimise energy efficiency and usage during the FY 2016/17.

Energy Reduction Actions

» Broad based installation of energy efficient lighting solutions with the use of LED, CFL and fluorescent tube lighting systems throughout the Company premises.

» Sharing printers, using high capacity toner cartridges and photocopy machines.

» Reduced energy consumption from the air conditioning cooling systems with the aid of UV repelling film and purchasing energy saving equipments.

» Periodic maintenance checks to ensure the efficiency and effectiveness of the electrical equipment in use and energy usage

» Strict monitoring on operating hours of the air conditioning system to ensure that central air conditioning is shut down after 5.00 pm

Energy Awareness

» Display of energy saving tips.

» Training programmes conducted for staff to increase awareness about the need to conserve energy and tips to save energy.

Employee Engagement

» Taking green practices home.

» Shared effort to cut down on use of lighting and equipment use.

☑ *G4-EN3*

Average Monthly Electricity Utilisation by MI from National Electricity Grid

	FY 2012/13	FY 2013/14	FY 2014/15	FY 2015/16	FY 2016/17
Head Office Electricity Utilisation (kWh)	49,962	52,829	53,070	55,609	51,652

Electricity energy consumption is measured in kilowatt hours (kWh). No major fluctuation has been observed in electricity consumption during the last five years

In order to substitute renewable energy options for non-renewable energy resources, MI is planning on introducing solar power technology to selected locations during the upcoming year, which will result in savings from electricity cost and contribution of energy to the national grid in the long term.

☑ *G4-DMA on Transport EN 30*

While electricity continues being the main source of energy, powering all MI premises, fuel is the other source used outside the Company in employee commuting, business related travel, and covering logistics between Head Office and branches. Considering the drawbacks resulting from burning fuel to the atmosphere, several steps have been taken to minimise the usage and emission levels as shown in the table G4-EN 4,EN5.

- Streamlined the vehicle maintenance process to ensure the energy efficiency and reduction of emissions, and obtained emission certificates for the fleet as per prevailing regulations.
- Obtained carbon footprint certificate by Sri Lanka Climate Fund for our vehicle fleet for FY 2016/17, and is working with the fund in moving towards neutral status.
- Encouraged alternative modes to reduce staff transportation.

☑ *G4-EN4, EN5*

Fuel Usage Trends:

Fuel	FY 2012/13	FY 2013/14	FY 2014/15	FY 2015/16	FY 2016/17
Petrol (litres)	213,902	263,022	323,828	405,000	552,509
Diesel (litres)	18,938	18,636	35,113	43,080	39,910

Energy Consumption Outside the Organisation :

Investigation Cost	FY 2016/17	FY 2015/16
Fuel (litres) used for investigations	223,812	157,690
Mileages	1,462,571	1,120,302

Energy Intensity

Energy Source	Consumption Level	
	FY 2016/17	FY 2015/16
Energy used within organisation (kWh)	619,824	667,308
Total Employees of Head Office	323	313
Energy Consumed per Employee Ratio (kWh per employee)	1,918.96	2,131.97

** Energy intensity is computed based on head office statistics.*

Controlling Fuel Consumption

MI's strategy towards sustainability, has resulted in initiatives to ensure that energy resources are used efficiently by the organisation.

Controlling fuel consumption of the Company's fleet of vehicles was initiated cognizant of the aim of minimising the impact on the environment. Our transport division monitors each vehicle and refers them to our own workshop for required periodic service to streamline the vehicle maintenance process which will ultimately ensure energy efficiency, the reduction of emissions, and lessen the environmental impact. Monthly reports are prepared to highlight the fuel usage by each staff member and submitted to the divisional head. Department heads are able to claim control over the usage of fuel and take necessary actions to bring down the fuel usage. Employees are encouraged to use fuel efficiently in planning their journeys, i.e., by pre-planning client visits and investigation visits in a way that the fuel usage is optimised.

Fuel usage by locations - Visit MI website

http://mi.com.lk/value-creation/value-creating-sixcapitals/natural-capital/

Management Discussion and Analysis

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Water Management

☑G4-DMA, EN8, EN9, EN10

Controlling Water Usage

The consumption of water for the basic needs of the workplace and employees' use is increasing, driven by the branch expansion and higher staff head count.

MI's engineering division has introduced specific measures at Head Office premises and at branch locations to reduce water consumption levels as part of our journey towards conserving natural resources. Tube-wells are set in the microfinance division and at Head Office and the usage of water is less, reducing the usage of water resources. Given that our operations do not consume vast amounts of water, our sustainability driven strategy currently does not consider reusing or recycling of water, but encourages employees to use water sparingly.

Average monthly water utilisation from National Water Supply :

	FY 2012/13	FY 2013/14	FY 2014/15	FY 2015/16	FY 2016/17
Head Office Water Utilisation (Units)	733	908	707	692	692

☑G4-DMA, EN22,EN23,EN24,EN25,EN26

Waste Management

As a Company carrying out business operations in the financial services sector, we do not discharge any waste water as a part of our operations. Our operations also do not result in significant spills of any kind. Thus, MI's core operations do not result in hazardous waste and spills and there is no direct impact on the environment. However, MI has taken proactive methods of disposing waste water, waste material such as garbage, e-waste and any other form of waste in a manner that does not harm the surrounding environment or contaminate ground water supply. We do not deal materially in waste deemed hazardous under the terms of the BASEL Convention and hence we abide to our standard disposal methods mentioned in the table below.

☑G4-DMA, EN15,EN16,EN17,EN18, EN19,EN20,EN21

Emissions

MI, in the face of climate change, is focused on managing risks and opportunities through the implementation of a strategy for mitigation and adaptation, where emission management has also become a major concern. We are working to understand and anticipate how changes in climate and the need for adaptation will impact not just our own business, but our customers and those companies we lend to, invest in, and purchase from. As MI provides financial solutions to customers in sectors that have negative impacts from climate changes, such as to the agriculture sector, MI as a consequence may also be exposed to indirect adverse effects, such as increased credit risk and non-performing loans.

We ensure that our emissions do not contribute to any climate change and significant preventive measures have been put in place. The tree planting campaign was one initiative that was kicked off to generate future carbon credits and our future plans on solar power generation is also another measure to minimise any negative impacts on climate change.

Placing of e-waste recycling bins at MI locations

Type of Waste Item	Frequency of Disposal	Disposal Method
1. Waste Paper	Weekly	Daily collection of waste paper from departments at Head Office is carried out at basement stores and disposed of on a weekly basis to an authorised party.
2. E-waste	Bi-annual	A separate storage area is assigned to store e-waste. Periodically, inventory is taken and quotations called for e-waste disposal with items being sold based on best price.
3. Damaged Office Equipment	Ad hoc	Damaged furniture, equipment and other similar items of various departments are forwarded to the maintenance department. The items are stored in Maharagama and sold when the realisable value is obtained with the approval of the management.
4. Polythene	Weekly	Daily collection of polythene taken from each department at Head Office is stored temporarily at a nominated location in the basement. Polythene is thereafter collected by the CMC.
5. Food	Daily	Collected daily at Head Office and disposed through the CMC garbage disposal process.

MI's Carbon Footprint

Collaborating with Sri Lanka Climate Fund, MI calculated the Company's carbon footprint levels from last financial year onwards and was appraised as a carbon conscious office. During the year, MI expanded its scope to cover all branch locations as well, which reaffirmed our commitment to a carbon conscious culture. The carbon footprint assessment carried out this year has been calculated based on the Green House Gas (GHG) accounting protocol of the World Business Council for Sustainable Development (WBCSD) and IPCC. The measurement of the CO_2 emission forms the point of origin for the Carbon Footprint Calculation, which is preceded by an extensive data gathering exercise that helps to ascertain the environmental imprint.

Carbon Footprint Intensity

The emission estimation of 2,447.27 tCO_2e cannot be compared against previous year, due to the expansion of the scope from Head Office to include all branches as well.

MI has made sufficient investment in green initiatives to earn carbon credits to offset carbon emission levels. MI has not emitted any ozone depleting substances and NOx, Sox and any other significant air emissions that include biogenic CO2 and are seeking to move towards carbon neutrality by 2020 through the Company's green initiatives, which include tree planting, promoting usage of eco-friendly vehicles based on hybrid/electric technology, and using energy efficient equipment. Currently, we do not assess emissions resulting from our lending business to those of our clients. However, MI is committed towards carbon neutrality in the forthcoming years, along with the projects focused on generating carbon credits.

Green House Gas Emissions Summary by Scope-2016/17

Scope	Type of emission	Emission Level tCO_2
Scope I	Refrigerant Gas Loss	64.09
	Emission from Business Purpose Travels & Employee Commuting - Investigation	522.10
	Emission from Employee Commuting	35.08
	Emission from Generators	6.37
Scope II	Emission from Electricity Consumption	470.42
Scope III	Emissions from Water Consumption (Drinking & Non-Drinking)	0.052
	Grid loss	36.19
	Emission from Business Purpose Travel and Commuting -Allowance	1038.12
	Emission from Commuting-Allowance	223.02
	Emission from Employee Commuting by Common and Private Transport	51.80
	Paper Recycling	0.03
	Total	2,447.27

Carbon Footprint Intensity

	FY 2016/17	FY 2015/16	Variance
Intensity Ratio (metric tonnes of CO_2e emissions per employee)	2.8 tCO_2e	1.8 tCO_2e	1 tCO_2e

Note: Scope 1, 2 and 3 and GHG emission (Carbon footprint) intensity computations have been based on Head Office and branches GHG emissions that include CO_2, N_2O, CH_4.

Greenhouse Gas Verification Statement
ISO 14064-1:2006
Sri Lanka Climate Fund

Chief Executive Officer
Sri Lanka Climate Fund

Management Discussion and Analysis

Natural Capital Review

☑ G4-DMA

Environment Protection

Green initiatives and other environment protective safety procedures have been implemented within the Company to preserve natural resources and the environment. Namely,

» Maintaining a Clean Business Environment
» Energy Management
» Water Management
» Controlling Consumable Intake
» Waste Management
» Conserving Biodiversity
» Tree Planting
» Monitoring GHG Emission Levels

Refusing and reducing usage of environmentally harmful resources while recycling and reusing resources is strongly embedded in our business practices, policies and has contributed to a more greener environment.

Key Green Initiatives 2016/17

ICT Goes Green

MI has attempted to identify potential environmental impacts in order that the Company could come up with ways to minimise the resultant negatives. The 'Green ICT' initiative is yet another programme driving our environmental conscientiousness. Our e-waste comprising of computers and related peripheral items is handled in an environmental friendly manner from procurement to disposal.

Virtual Servers

More than twenty application servers are being hosted on three physical servers. Through this measure, we save on energy, as we reduce the number of servers required.

Reducing Paper Usage

The Company's e-mail system, core system modules and document management system among others, facilitate users to view documents online and limits the need of printing hard copies as practically possible. Hence, at least 40,000 A4 sheets are saved per month.

Using Energy Efficient Computer Equipment

MI has enhanced its procurement strategy to ensure that energy efficient devices are purchased and configured with energy saving settings. Further we have started purchasing mini PC systems, which will result in major savings of power consumption.

Video Conferencing

The Company is carrying out testing to schedule corporate meetings through the use of video call conferencing with branches, which will reduce travel time, accommodation and fuel cost.

Environment and its Habitat Protection Projects Executed

Tree Planting Project

On 31st March 2017
By the Sustainability Governance Committee

Project Rationale

To support in creating a greener environment through tree planting campaigns which will help reduce global warming for future generations, while reducing our carbon footprint.

Project Action

The Sustainability Governance Committee jointly with the 'Rotary One Million Tree Trust (Gte) Ltd' carried out a tree planting campaign for the second time, this time in Bathalagoda Wewa in Kurunegala. Managers and staff members voluntarily participated in this worthy cause.

Contribution

Monetary Value – Rs. 89,000 (Budgeted – Rs. 200,000)
Management Time – 50 hours
Staff Volunteerism – 70 hours
In-kind Assistance – N/A
Number of Beneficiaries – N/A

☑ *G4-DMA, EN11, EN12, EN13, EN14, EN26*

Biodiversity Management

With the expansion and enhancement in business operations around the country, MI has focused its attention on the surrounding environment and especially on selected biodiversity locations. Having minimal impacts on the environment due to the nature of our business, we have ensured through an initial assessment and subsequent audits that our operations do not harm designated protected areas of national conservation or areas of high significance in terms of biodiversity. Moreover, we have taken proactive measures to mitigate the indirect impact on the environment by being more conscious about whom we extend credit facilities to and avoid or limit any facility being granted to any person or organisation which generates adverse impacts on the environment. Based on assessment of information originating from all our operating centres, and evaluating the branch/service centre proximity to demarcated areas of biodiversity of the country, only one branch falls within the 3km radius from a designated site. However, these protected sites are not affected in any manner from our operations.

Biodiversity Location-wise - Visit MI website

http://mi.com.lk/value-creation/value-creating-sixcapitals/natural-capital/

☑ *G4-DMA, EN32,EN33*

Supplier Assessment

As a finance company, our business operation is more customer driven with insignificant dependence on suppliers and therefore, we have not extended our environmental assessment to suppliers for their environmental footprint.

☑ *G4-EN29*

Environmental Compliance

Despite the minimal operational impact, MI as a responsible corporate citizen continues to embrace global best practices on environment governance, while complying with legal requirements. There were no violations reported for the FY 2016/17, on any environmental standards and the Company was not called upon to settle any environmental related fines. No sanctions were imposed as a result of non-compliance with any environmental regulations during this period. Assurance to this effect is provided on page 275 in the Statement on the Annual Report of the Board of Directors. Going beyond our own compliance standards, we hope to bring in environmental policies that pertain to our customers to encourage them in turn to adhere to environmental regulations by strengthening our prerequisites for granting of credit facilities.

☑ *G4-EN34*

Environmental Grievance Mechanisms

We continued to implement suitable remedies to resolve any adverse impacts resulting from MI's business operations on the environment.

A feedback form affixed to the Annual Report is available for any party to convey environmental concerns resulting from our operations, which will be looked into by the management depending on its materiality. No environment related grievances were reported to management formally during FY 2016/17, and there are no grievances brought forward from previous year requiring resolution.

☑ *G4-EN31*

Expenditure on Environmental Protection

Environmental Protection Initiative	Activity Involved	Expense for FY 2016/17 Rs.
Green Initiatives		
Tree Planting Investment	Planting of trees in Bathalagoda Wewa in Kurunegala	89,000
GHG Emission Testing	Annual emission certificates obtained for MI fleet of motor vehicles and other office items	267,750
Opportunity Cost of Employee Volunteerism	Staff members and managers spent 120 man hours for green initiatives	69,880

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S.B.Ekanayake
Principal

☑ *G4-DMA, S01, S02, FS 13, FS 14*

Our Approach to Social Capital Value Creation

In recent years, social capital creation has become a key component in our business model, in defining who we are and how we operate as a responsible corporate. From a visionary perspective, we envisage becoming a social partner to communities, manoeuvring our business to reach-out and fulfil the untapped financial needs of society, and also cater to other social needs of the poor and less privileged. As we forge ahead in our commercial activities, cementing lasting business relationships with people, we are committed to going that extra mile in catering to the varying partially met and/or unmet needs of society, having deepened our impact on society year after year. Having widened our footprint during the last decade, we stand much closer with people of all communities, to detect and fulfil a wide variety of untapped social needs. The full benefits of these voluntary efforts executed across our operation, will accrue to society and indirectly to MI, more effectively from a long term perspective. Each year, we evaluate the impacts that we continue to create on society, so that identified gaps can be bridged to the satisfaction of all those in need. Such acts of thought and foresight give us the social license to operate within the communities we operate in.

http://mi.com.lk/value-creation/value-creating-six-capitals/socialcapital/

Key Performance Indicators

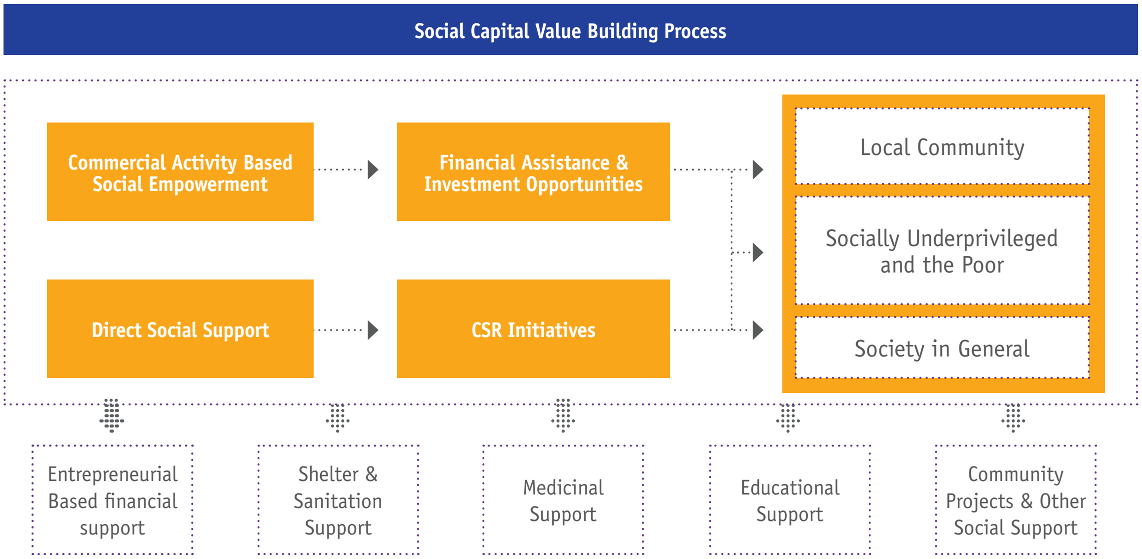
	Actual 2016/17	Actual 2015/16	% Change
Social Capital Impacts;			
Number of Beneficiaries	4,218	719	487%
Total Microfinance Lending (Rs. Mn)	1,202	560	115%
Senior Citizen Deposits (Rs. Mn)	9,576	7,650	25%
Operations Assessed for Risk Related Corruption (Number)	9	9	0%
Total Investment in Community Projects and Social Support (Rs. 000)	2,046	7,053	-71%

Capital Objectives

- To be in the forefront of creating a sustainable future for all.
- Increase MI's social footprint annually.

Future Goals

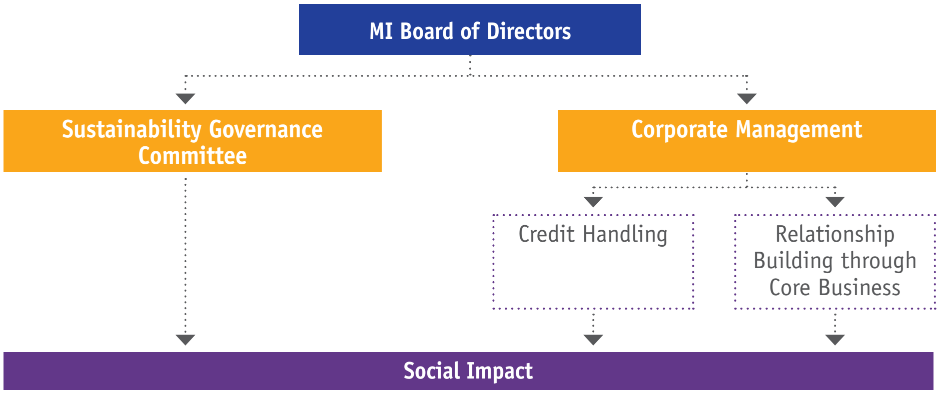
- Beneficiaries of social initiatives beyond financing to increase by 20% year-on-year.
- To widen micro finance empowerment by 20% before the next financial year.



Management Discussion and Analysis

Social Capital Review

Social Handling Operational Structure



Policy on Social Capital Value Building

Our policy on social capital value building is to operate in a way that will bring greater value to society as a whole, one that will result in a win-win situation for society and the Company alike. We expect to widen our impact on society as we continue as a responsible corporate citizen, going that extra mile to fulfil dreams of people. Accordingly, it is our expectation to bring MI's broad ranging financial solutions to people living in different parts of the nation. We hope to maintain close interaction with untapped customer segments of society, low income earners and the poor, by improving their lives and livelihoods through our products and services that all aim to deliver financial independence by breaking the shackles of poverty. We will also travel that extra mile to help people with our philanthropic activities.

Working Structure

The overall responsibility for building social capital value like all other capitals lies with the MI's Board who stands committed in making reality its value enhancing aspirations. While taking a supervisory role, the Board in-turn has delegated its responsibilities to the Sustainability Governance Committee to work closely with all members of the corporate management team to carry out frequent assessments on societal expectations and look for ways of satisfying them.

Stakeholder Survey results - Visit MI website.

http://mi.com.lk/value-creation/value-creating-six-capitals/socialcapital/

From a commercial perspective, the core business divisions are expected to reach-out from all geographic locations to offer tailor-made solutions and attractive investment options in the process. Front line divisions are expected to remain receptive to people's preferences and changing expectations overtime. Moreover, the Sustainability Governance Committee is entrusted with a much larger role in directly identifying needs of society, focusing more on the poor and less privileged and working for the well-being of communities in general.

Our Social Investment

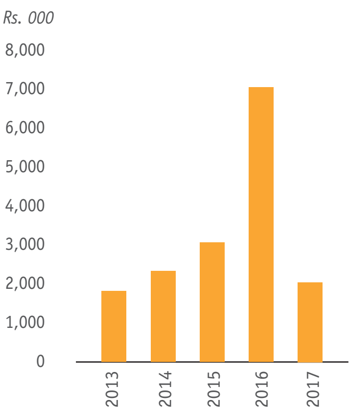
We work within a fixed budget to carry out more focused and direct societally benefiting initiatives, and also through general philanthropic support assisted people to better their lives. The total social investment for this period stood at Rs. 2 Million with a wider coverage, and also our social efforts did not only come in monetary terms but also involved management's time in identifying, expediting and following up on activities of a social nature.

☑ G4-FS7

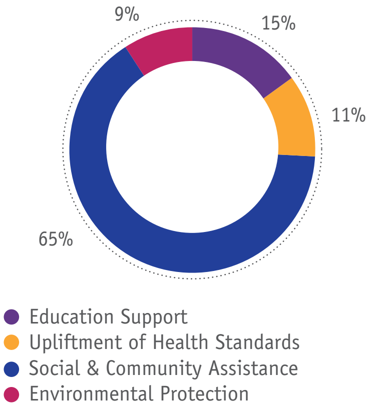
Commercial Activity Based Social Empowerment

Through the relationship capital building process explained on pages 95 to 105, we were firstly successful in servicing a relatively higher customer base than last year, attracting new clientele whilst continuing to satisfy the needs of our existing customers. This paved the way for us to further cement bonds with people, in being a supportive financial partner in their own development

Community Investment



Aspects of Community Investment



and economic prosperity. In particular, our microfinance business penetrated right into the very heart of communities, empowering communities in many ways to better their lives and livelihoods. We managed to provide immediate funding to lower income earners through the microfinance centres housed in more than 20 MI locations across the country. We dealt with over 1,300 micro-based centres in the process, which brought together unprecedented level of women from varying communities, empowering them along with their families to start-up their entrepreneurial abilities, increase their earning capacities and enjoy economic freedom. Our actions contributed to more self-employment activation in the country, creating greater employment opportunities and increasing per capita income.

Through the expanded branch network, we continued to offer additional returns to our deposit holders who are senior citizens and provided all investors a gateway to deposit their savings, which continued to provide them with attractive returns. All those who transacted with us were subject to a total value added experience that encompassed our unique personalised service that included speed, convenience and much needed empathy.

☑ *G4-DMA on anti-corruption, SO3, SO4, SO5*

Culture, Ethics and Compliance

Carrying out our business activities in a professional, responsible and ethical manner, ensuring that we comply with all regulatory and statutory requirements and implementing best-in-class industry practices and governance techniques to prudently manage our business in safeguarding public money and all other key interests of our stakeholders are enshrined within our governance philosophy. Our business operations did not in any way negatively impact local communities that we continue to operate in. MI adopts strong internal control systems with adequate oversight by the audit function which is able to review areas of non-compliance, fraud or corruption on a regular basis and report to the Board Audit Committee. Our internal value system requires that all our employees employ ethical practices while the Company acts as fair competitors in the industry, not denigrating other firms when carrying on its business activities.

As a leading finance company that dates back to the sixties, MI actively participates in key commercial associations that have been formed for the common interest of all firms in the sector. We have contributed to the development of the financial services sector by way of our organisational growth and expansion of services and by raising sector standards.

MI Lending having direct positive social impact

Initiatives	Target Social Group	Number of Customers Served	FY 2016/17 Rs. '000
Microfinance	Low Income Earners	26,956	1,201,555
Senior Citizen Deposits	Senior Citizen Clients of MI	2,519	9,575,546
Riyadiriya	Low Income Earners	2,093	703,585

MI's core business operation impact as a percentage of population

	FY 2016/17						
	Eastern	North Central	North Western	Sabaragamuwa	Southern	Western	Central
Number of Branches	2	3	3	4	5	18	1
Number of New Branches	-	1	-	-	-	3	1
Population	1,555,510	1,266,663	2,380,861	1,928,655	2,477,285	5,851,130	2,558,716
Lending Customers /Deposit Customers	578	5,124	5,712	6,260	4,849	21,212	64
Lending Customers /Deposit Customers (% of Population)	0.04%	0.4%	0.24%	0.32%	0.2%	0.36%	0.0%

Source: Population on 2012 Population Census Statistics

Management Discussion and Analysis

Social Capital Review

Anti-Money Laundering Policy (AML)

MI's Board approved the revised anti-money laundering policy document during the year which incorporated the Money Laundering Risk Management Gazette 2016 requirements. A dedicated full-time compliance officer is entrusted with the responsibility of implementing requirements of the Financial Transactions Reporting Act (FTRA) and other regulations issued by the Financial Intelligence Unit and to monitor and report to the Board on related matters. Accordingly, based on these AML policies and procedures, respective divisional staff are expected to maintain high standards on customer identification, KYC, due diligence, record keeping, reporting obligations, etc. During the period, employees attached to front-end, as well as back-office were subject to in house training on mandatory AML legislation and related procedural requirements.

Anti- Corruption Policy

The Board approved "fraud and whistle-blowing policy" which was implemented in 2013 continues to be a formal reporting process that is available to staff whenever they come across any incidents of fraud and corruption that remain undetected or unresolved. The head of audit apprised employees of the importance of this document together with the channels available to report incidents. The internal audit team worked closely with the Audit Committee to detect and report shortcomings and lapses in internal procedures including incidents of corruption.

During the FY 2016/17, there were no money laundering related incidents carried out by any external parties nor were there any incidents of corruption reported.

Operational risk assessment on anti-corruption

	FY2016/17	FY2015/16	FY2014/15
Total number and percentage of operations assessed for risk related to corruption	9 100%	9 100%	8 100%
Significant risks related to corruption identified through the risk assessment	0	0	0

☑ *G4-SO8*

Compliance with Laws and Regulations

The Board of MI, the Board Committees, and management committees together with the compliance officer continued to monitor MI's adherence to prevailing laws and regulations and took steps to bridge any gaps that were prevailing during the year. Any notable lapses in compliance were taken up and resolved with respective departmental heads and staff concerned.

Except for the non-compliance matters given in note no. 22, to the Financial Statements in page 318, and note no. 53 in page 354 on liquidity, there were no non compliance or significant fines or any non-monetary sanctions imposed on the Company for breach of laws and regulations.

☑ *G4-SO11*

Handling Societal Grievances and Negative Societal Impacts

There were no formal reported instances of social grievances or negative impacts related to society, for the year under review and also no grievances were brought forward from last year for follow up. A feedback form is affixed at the end of this Annual Report, which may be used by any member of society, having experienced any grievance due to MI's business, to convey concerns to the Board and management of the Company.

Direct Social Support

As a corporate citizen that understands societal needs, we strived to help people of all communities, especially the poor and the underprivileged. Through direct communication and our own sources, we tracked down those lacking basic necessities ranging from shelter to educational support and community service and assistance in times of crisis. MI's Sustainability Governance Committee led by example, initiating these worthy social projects focusing on some of the 'burning issues' of society. We concentrated on helping the poorest of the poor and also supported by way of various community projects for the betterment of society. We also believe that being part of a fully-fledged tree planting project plan starting from this year, would certainly benefit society in building a more sustainable living environment for people. Out of the planned 14 CSR projects, the Committee successfully completed all projects except for the house building project commenced in Thissamaharama which is ongoing and will be completed by early next financial year. This reflected a 93% (2015/16 - 83%) successful completion rate.

Social Initiatives Pursued – FY 2016/17

Mercantile Investments & Finance PLC through the efforts of the Sustainability Governance Committee and its support staff, undertook a number of invaluable projects for the benefit and well-being of society during the FY 2016/17. Given below is an outline of all such projects and other related social initiatives and assistance extended.

Flood Relief

On 25th May 2016
By the Sustainability Governance Committee

Project Rationale
Help to provide shelter, food and comfort to families affected by flood, and support rebuilding of their lives.

Project Action
Dry rations were provided to flood victims in the suburbs of Colombo. The microfinance team played a key role in helping these under privileged families.

Contribution

Monetary Value – N/A (Budgeted Cost – N/A)

Management Time – 500 hours

Staff Volunteerism – 3,750 hours

In-kind Assistance – Dry Rations (Rs. 200,000)

Number of Beneficiaries – 2000

Drought Relief

On 27th January 2017
By Microfinance Division and all MI staff members

Project Rationale
Provided dry rations to families affected by the drought.

Project Action
All staff of MI contributed to raise funds in supporting people who were affected by the drought. The microfinance customers who faced the crisis were assisted by this project.

Contribution

Monetary Value – N/A (Budgeted Cost – N/A)

Management Time – 100 hours

Staff Volunteerism – 40 hours

In-kind Assistance – Dry rations (Rs. 125,500)

Number of Beneficiaries – 100

House Building Project

On 3rd February 2017
By the Sustainability Governance Committee

Project Rationale
To assist a microfinance family in the Tissamaharama area, who lived in a dilapidated house and were constantly under threat of attacks by wild elephants.

Project Action
The Sustainability Governance Committee initiated building of a house for this family. The construction is ongoing and completion is to take place next financial year.

Contribution
Monetary Value – Rs. 244,500 (Budgeted – Rs. 300,000)
Management Time – N/A
Staff Volunteerism – 60 hours
In-kind Assistance – N/A
Number of Beneficiaries – 3

Management Discussion and Analysis

Social Capital Review

Donations to Apeksha Hospital in Maharagama

On 5th October 2016

By the Sustainability Governance Committee

Project Rationale

Improve efficiency and effectiveness of patient care services at Apeksha Hospital in Maharagama.

Project Action

The Sustainability Governance Committee donated five commode chairs to Apeksha Hospital (a transit hospital) on 5th October 2016, with the intention of improving the standard of patient care service. As a large number of cancer patients from all over the island are treated at Apeksha Hospital, we believe that our donation would assist the lives of such cancer patients.

Contribution

Monetary Value - N/A (Budgeted Cost – Rs. 70,000)
Management Time – 9 hours
Staff Volunteerism – 9 hours
In-kind Assistance – 5 Commode chairs (Rs. 60,500)
Number of Beneficiaries – 800

Donation of Drinking Water Facility to a School in Kurunegala

On 15th December 2016

By the Sustainability Governance Committee

Project Rationale

Facilitate rural school children with clean drinking water.

Project Action

Financed installation of drinking water facility and donated steel cupboards for Bogasboballa school in Kurunegala.

Contribution

Monetary Value – Rs. 36,999 (Budgeted – Rs. 95,000)
Management Time – 90 hours
Staff Volunteerism – 0
In-kind Assistance – Cupboards (Rs. 52,957)
Number of Beneficiaries - 104

Donations to a School in Kosgama

On 18th November 2016

By the Sustainability Governance Committee

Project Rationale

Aiming to widen the opportunity to build the sports background of underprivileged children in Bollathawa School, Kosgama.

Project Action

A request for assistance by the Bollathawa school were met when MI donated variety of sports goods including volleyballs, netballs, footballs, badminton sets, carrom boards, chess boards, tennis balls, etc., for the use of school children.

Contribution

Monetary Value – N/A (Budgeted Cost – Rs. 35,000)
Management Time – 6 hours
Staff Volunteerism – 12 hours
In-kind Assistance – Sports Goods (Rs. 31,962)
Number of Beneficiaries - 114

'Adopt a Dog in Sri Lanka' –Sterilisation Camp in Pannipitiya

On 25th November 2016
By the Sustainability Governance Committee

Project Rationale
To support animal welfare through the 'Adopt a Dog in Sri Lanka' a non-profitable organisation driven by a group of passionate volunteers.

Project Action
MI made donations to 'Adopt a Dog in Sri Lanka' enabling them to contribute to the welfare activities of animals. The campaign was carried out in Pannipitiya, mainly focusing on sterilisation and vaccination of dogs and cats.

Contribution
Monetary Value – Rs. 60,000 (Budgeted – Rs. 70,000)
Management Time – 8 hours
Staff Volunteerism – 6 hours
In-kind Assistance – N/A
Number of Beneficiaries – 75

Eye Checkup and Eye Donation Camp for Microfinance Clients

On 6th December 2016
By the Sustainability Governance Committee

Project Rationale
Extend support to the low income families of Microfinance clients at Mercantile Investments & Finance PLC.

Project Action
An eye check-up and eye donation campaign was carried out through the Ratnapura and Horana branches of MI together with Vision Express Optometry Company Ltd. The campaign reached out to people including staff members, where participants were educated on eye diseases and related problems. Thereafter, 5,000 leaflets were distributed to microfinance clients as an awareness campaign.

Contribution
Monetary Value – Rs. 20,845 (Budgeted – Rs. 20,000)
Management Time – 72 hours
Staff Volunteerism – 168 hours
In-kind Assistance – N/A
Number of Beneficiaries – 630

Management Discussion and Analysis

Social Capital Review

Other Social Projects - FY 2016/17

By whom	Date	Description	CSR Activity	Budgeted Cost (Rs.)	Actual Cost (Rs.)	Number of Beneficiaries	Impact
Sustainability Governance Committee	June 2016	Donation for the National Seminary Philosophate Library Refurbishment	Donations made for a noble cause by providing necessities to upgrade the library at 'National Seminary of Our Lady of Lanka'.	25,000	20,000	30	Through aid given to the library, enabled them access to information.
Sustainability Governance Committee	June 2016	Donation of school items for flood affected school children	Shoes, school bags and other stationery items were donated to two school children.	10,000	9,007	2	In their time of need, MI came to their assistance with school supplies enabling them continue with their education.
Sustainability Governance Committee	December 2016	Donation for a spine correction operation	Funds provided for an operation to correct the spine of a child.	20,000	25,000	1	This assisted the child who is of school going age in helping her to lead a normal life.
Sustainability Governance Committee	January 2017	Donation to an Elders' Home	Emergency lamps and cupboards were donated.	40,000	39,215	50	The donations helped the elders' home meet basic needs like lighting.
Sustainability Governance Committee	October 2016	Releasing of cows	Releasing cows and handed over their custody to low income families.	55,000	50,000	9	Low income farmers were assisted to improve their economic standards.
Sustainability Governance Committee	November 2016	Sponsoring an awareness campaign	Donations made to 'Sri Lanka Sumithrayo' a charity organisation, for the materials needed to carry out awareness campaigns to assist suicidal and despairing persons.	60,000	60,000	300	Assist suicidal and despairing persons to cope better.

Other Assistance to Society

Date	Party supported	Description of social activity performed	Actual Cost (Rs.)
April 2016 - March 2017	Donations given to school clubs & societies	Raising funds for the schools welfare	162,000
April 2016 - March 2017	Donations given to other institutions	Raising funds for various activities organised by these institutions	31,000
April 2016 - March 2017	Miscellaneous Parties	Donations given to various other parties	594,520
April 2016 - March 2017	Religious societies	Giving financial support to these societies with regard to religious events organised	208,000
17th February 2017	Sri Lanka Sumithrayo, Colombo	Donation for fund raising event	25,000
23rd November 2016	Welfare Society Magistrate court, Mathugama	Donation given for the annual sports meet	25,000
Total			**1,045,520**
Total cost of community projects and social support			*2,045,512*
Total expenditure on community projects and social support as a percentage of post-tax profits			*1%*

External Sustainability Charters

☑ *G4-15*

Global Compact Considerations

As a voluntary exercise, the Company draws reference to the Global Compact Considerations to enhance and benchmark its efforts towards building a more sustainable society and environment. This has enabled the Company to become more aware of some of the key areas of sustainability focus, which has become another cornerstone in improving our current sustainability polices, practices and processes. Given below is MI's extent of adoption of the 10 key principles of the Global Compact Considerations upheld by the United Nations Global Compact (UNGC), which covers the areas of human rights, labour, environment and anti-corruption.

Global Compact Considerations 10 Principles			MI's Extent of Adoption in FY 2016/17
Human Rights	1.	Businesses should support and respect the protection of internationally proclaimed human rights.	In combination with our internal value system that upholds people's rights and obligations, we continued to adopt effective HR policies, practices and procedures which are aligned with standard human rights requirements. Major business decisions were made without compromising on key obligations related to the human rights of employees and general external factors.
	2.	Make sure that they are not complicit in human rights abuses.	There were no reported incidents of human rights abuses or violations during the period under review. MI remained a caring and receptive employer when managing its workforce and upholds the criteria of basic human rights necessities of the human resource. Our dealings with external parties such as our customers, suppliers, and other external parties is carried out in a humane manner, without going against basic human rights considerations.
Labour	3.	Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining.	MI's management style and culture encourages communication of employee views and concerns to be transmitted freely without obstruction to those at the helm. Employees' feedback to corporate management is deemed invaluable and constructive information and hence, viewed positively. Having established effective HR policies that include grievance procedures, the management is able to iron out human resource concerns, paving the way for a more harmonious relationship with its workforce.
	4.	The elimination of all forms of forced and compulsory labour.	As a strict HR policy, we do not employ people forcefully under any circumstances.
	5.	The effective abolition of child labour.	The Company recognises the importance of ensuring that children are not employed in any capacity whatsoever and abides strictly to this requirement.
	6.	The elimination of discrimination in respect of employment and occupation.	There is no form of discrimination taking place with regard to an employee's age, sex, ethnicity or religion. The appraisal system practiced is performance based and thus, any rewards and benefits generated from such evaluations purely focus upon an employees' capabilities and most of all his/her performance during a period.
Environment	7.	Businesses should support a precautionary approach to environmental challenges.	As a responsible corporate citizen MI continued to embrace a green policy, practices and procedures to safeguard its external surroundings and reduce the use of natural resources. The Company also expanded its efforts in preserving the environment and its habitats.
	8.	Undertake initiatives to promote greater environmental responsibility.	The efforts of the Sustainability Governance Committee, in identifying ways of contributing to the sustenance of plants and the animal population can be seen as wider actions supporting this principle.

Management Discussion and Analysis

Social Capital Review / Future Outlook

Global Compact Considerations 10 Principles			MI's Extent of Adoption in FY 2016/17
	9.	Encourage the development and diffusion of environmentally friendly technologies.	The continued use of environmental friendly internal procedures and practices helped better manage the use of natural resource such as energy and also to reduce emissions to the atmosphere. Efforts this year in tying up with an external party under agreement to handle the Company's e-waste has been another major step towards adopting this principle. Plans on converting MI's Kohuwela vehicle servicing plant to solar power, in combination with the national grid is currently being evaluated.
Anti-Corruption	10.	Businesses should work against corruption in all its forms, including extortion and bribery.	In keeping to MI's sound governance framework and culture, all individuals working within were expected to display highest degree of integrity, honesty and ethical standards. Action was brought upon employees who did not conform to the high standards set. The "Whistleblowing and Fraud Policy" approved by the Board would assist the Board and management in identifying any future corruption, fraudulent activities, etc., occurring in the workplace and it has laid a sound foundation to initiate action against those responsible for any fraudulent acts. It sets a clear process to capture related concerns and then to investigate, report and take corrective measures against wrongdoers.

Future Outlook

As a nation steadily progressing with development of the economy, the future looks optimistic for all those willing to take on the challenge. The business community is on a sound footing, to take advantage of the forward looking economic policies set-forth to bolster the industry and services sectors. The positive changes happening together with the international community and pick up seen in international trade deals would also play a significant role in accelerating GDP growth, which is projected at around 4.7% 2017-2020 in the medium term. Inflation is expected to remain within single digits for the next few years, but is expected to take an upward trend. It is expected that the Rupee would further depreciate against major currencies, but not steeply as in the past and therefore, having minimal impact on import costs. However, the prevailing application of high duty on importation of motor vehicle imports is likely to continue into the future, and will remain a challenge for the vehicle sales market. Despite the drawback, the prevailing high market interest rates structure is sure to reverse within the next two years, gradually stimulating economic activity.

The finance company sector credit growth nevertheless will remain pegged back on account of the credit control measures already enforced by the Government, but the industry's core margins are expected to improve once interest rates start taking a downward trajectory. In driving the loan book, greater emphasis will be placed by finance companies in developing its non-vehicle backed lending, which currently has no major regulatory barriers. In terms of mobilising investments, the projected increase in per capita income and the increasing savings habit of the people will drive the industry's fixed deposits and savings products in the medium term. Nonetheless, greater improvisation will be required by the industry in sustaining business as a general ingredient, especially to counter the stiff competition within the industry and also from the banking sector.

The impact of digitisation which is being driven by the Telcos and being fast adopted by the banking sector is the next chasm the NBFI's would have to cross. Convenience and ease of access through the use of the smart phone is a rising customer expectation with the onset of e-banking platforms, electronic payment gateways, the automation of the interbank payment system and near field communication developing rapidly with the banking and insurance sectors being early adopters.

The persistent leasing book growth recorded is likely to get pegged back with the recent restrictions on the loan-to-value maximum ratios applied, but to the contrary, property backed lending, microfinance and other forms of un-collateralised forms of lending are bound to escalate, as a means of fulfilling anticipated volumes targets. As a consequence we can expect overall yields of the sector to improve exponentially, but profitability will remain somewhat impacted due to increased impairment charges arising due to such forms of credit being lower on asset quality. The industry tax costs will increase compared to the preceding year, primarily due to the 4% increase in the financial services VAT and the resultant impact on the corporate tax taking full effect.

Management Discussion and Analysis

Future Outlook

Our Future Approach

The wider changes taking place in the business environment, not only expands business opportunities for us, but will also bring about a fair share of challenges that is bound to impact the Company, when developing our future capital value.

Future Predictions Impact on MI	Key Future Strategic Priorities	Future Approach
Financial Capital		
Expected Positives; » Once interest rates upward trajectory movement reverses possibly within the next two years, MI's deposit cost of funding will decline over time, resulting in improved margins » As more emphasis will be given to develop our non-traditional lending, overall yields and margins will improve further going forward **Expected Negatives;** » New credit control measures will peg back lease revenue growth temporarily » The full effect of increased VAT rate and corporate tax effect will impact post tax profits commencing in the new financial year » Increased exposure to non-vehicle backed lending will increase asset quality risk	» Record sound annual growth in post-tax profits » Maintain overall spread above 8% by increasing yields and sourcing cheaper funding » Annual collections ratio to be above 90%, while keeping the non-performing lending ratio below 4% » Bring down the assets and liability one year mismatch below Rs. 2 Billion » Bring down the cost to income ratio below 55%	**Optimising Core Margins** Traditional financing will be coupled with term based higher yielding products to keep yields high. In sourcing funding at optimal costs, fixed deposits will be extensively promoted in tandem with low cost savings. We will also pursue higher levels of medium term borrowings as a means of controlling maturity mismatches. We will not limit this to local options, and pursue international funding avenues as well. **Controlling Expenditure** In the midst of expansion, capital expenditure will be tightly monitored. Overhead costs stemming from strategic business units and departments will be constantly reviewed, towards cost optimisation and elimination of wasteful expenditure if any. **Managing Asset Quality** We hope to implement the planned internal credit rating system within the next year to enhance credit evaluation of our clients. Through a strong recovery drive, we will improve efficiency levels relating to daily collections and expedite action on problematic accounts.
Relationship Capital		
Expected Positives; » Steadily improving economic conditions will enrich people, their purchasing power and need for credit to drive their livelihoods » Expanded presence will broad-base and nurture lasting customer relationships to develop **Expected Negatives;** » Competition within LFC's and indirect competition from banking sector would continue to be intense » Stringent credit control measures applied together with a somewhat stagnant vehicle sales market will pose further challenges in increasing existing business volumes and generating new business	» Increase both lending and deposit customer acquisitions and new business by 12% and 15% respectively » Lending book growth to be maintained above 12% and deposit base growth to be 15% » Increased economic value addition and distribution to employees, suppliers and to Government as taxes	**Widening Branch Relationships** We plan to exercise our dominance, increasing our customer partnerships through the branch network. We hope to consolidate our position in recently established regions so that we can cater to a larger cross section of people. Microfinance operation will play a vital role in the outskirts of Sri Lanka, in tapping the needs of the poor and middle income earners. The product mix will be enhanced further to fulfil these broader needs of people. **Unique Customer Experience** With the proposed system changes that are to come into effect next year, some of the key operational process will be re-engineered. This is to facilitate customer convenience when transacting. Future staff training will go hand-in-hand with this decentralised approach, with the intent of improving existing service standards and service quality.

Management Discussion and Analysis

Future Outlook

Future Predictions Impact on MI	Key Future Strategic Priorities	Future Approach
Human Capital		
Expected Positives; » The Workforce will be well conversant with the ever changing regulatory environment, and equipped to handle future demands of the industry and customer base **Expected Negatives;** » Rising competitive job opportunities, in line with the expanding industry size » Will be subject to resistance and other challenges when planned structural changes take effect » Employee motivation and morale will be somewhat dented with increasing job demands	» Drive employee productivity levels upward within the next 15 months » Increased training hours per staff member to a minimum of 10% » New recruitments to workforce to exceed 100, with majority as marketing assistants, recovery staff and deposit officers	**Total Performance Driven Culture** We hope to extend our performance driven culture to all divisions of the Company and plan to obtain services of an external consultancy firm to evaluate our human resource capabilities against future requirements and to recommend areas to improve performance. **Talent Development** We hope to intensify staff training and development activity which will be an imperative tool in grooming individuals to face the business complexities of the future. Assistance will also be sought from external training experts to cover technical training, group activity, improving basic linguistic skills and presentation skills and also focusing on team building and personality development.
Intellectual Capital		
Expected Positives; » Our expertise and know-how will drive competitive advantage and stay innovative in developing new products and distribution channels to capture new business and penetrate existing and new customer segments **Expected Negatives;** » High propensity for competitors to also make innovative changes, embracing technology and other competitive factors » High initial investment outlays in proposed technology changes could hamper short term profitability	» Building the "MI" brand and creating visibility across all viable locations » Embracing an ICT framework that encompasses advanced technology features and drives customer convenience » Acquire business intelligence and enhance knowledge and skills of workforce for differentiation and competitive advantage	**Brand Awareness Campaigns** Through the Senior Manager Branding, we plan to intensify our brand development activity across the island, with an adequate budgetary allocation to support such initiatives. **Migration to Advanced ICT System** We hope to fully migrate to the acquired external ICT system within the next 12 months that will provide a wider spectrum of features for users, which incorporates capabilities to meet future needs. In-house ICT teams will be guided and assisted by the IT Consultant during the implementation phase, and post implementation with adequate training and advice. Users will receive the required system training support, post implementation.

Future Predictions Impact on MI	Key Future Strategic Priorities	Future Approach
Social Capital		
Expected Positives; » Expected future expansion and deeper market penetration gives adequate opportunity for us to increase societal interaction, to identify untapped needs of society **Expected Negatives;** » A time lag in generating new leads and community/customer needs identification will be inevitable due to the new branches in the network requiring time to get a firm foothold in the communities they operate in	» Supporting communities to better their lives and livelihoods by growing the loan book outside the Western Province by 15% » Increase our community assistance programmes at least by 10%, beyond commercial boundaries	**Financial Empowerment Plan** Over the next three years, we hope to widen the scope of our financial services, playing a larger role outside the Western Province, particularly through our microfinance business and personal loan products, to empower communities and to transform their lives for the better. **Supporting Community Development** We expect to continue the social based assistance and community service that we provide the poor and the less privileged, going beyond our commercial operation. Through wider links with local communities, we hope to make a larger positive impact on society and obtain a social license to operate within these communities which in turn will contribute to increasing our brand value. **Employee Welfare** We will complete development of the fully fledged canteen for our Head Office staff and focus on ways of widening staff welfare.
Natural Capital		
Expected Positives; » The foundation laid to track MI's impact on the environment and its importance will provide the needed impetus for us to pursue environment protection activities **Expected Negatives;** » The need to consider environmental protection requisites becomes greater as branch expansion continues and cannot be ignored	» Instil the "green focus" concept across all branches and in all employees » Increase our investment towards protecting the environment and its habitats by minimum 10% year-on-year	**Curtail Natural Resource Usage** In the wake of operational expansion, our usage of energy, stationery and other naturally produced consumables will increase and henceforth, we will establish strong control mechanisms to optimise use, re-use and recycle where possible and reduce wasteful usage and monitor progress. The possibility of utilising solar power in combination with the national grid energy will be explored for few selected locations. We also hope to evaluate and move into an advanced eco-friendly air conditioning system, replacing the existing central air conditioning system at the Head Office. **Environment Protection** We hope to utilise our growing wildlife fund and also the CSR budget to initiate programmes that will better protect plants and the animal population with specific focus on looking after the well-being of injured animals and endangered species. We hope to also pursue our tree planting campaign for the second consecutive year with the Rotarians.

GRI G4 Content Index: 'In accordance' - Comprehensive

General Standard Disclosure:

G4 index	Description of Disclosure required	Disclosure given section/ remarks	Page number	If disclosure is omitted, reason for omission	Externally assured
	Strategy and Analysis				
G4-1	Statement from the Chairman	Chairman's message	16 to 21		Yes
G4-2	Description of key impacts, risks and opportunities	Management Discussion and Analysis	55 to 62 & 64 to 67		Yes
	Organizational profile				
G4-3	Name of reporting organisation	Mercantile Investments and Finance PLC			Yes
G4-4	Primary brands, products and/or services	About us	33 & 34		Yes
G4-5	Location of the organisation headquarters	236, Galle Road, Colombo 03, Sri Lanka.			Yes
G4-6	Countries where the organisation operates, has significant operations or that are specifically relevant to sustainability topics covered	Operations carried out entirely in Sri Lanka.			Yes
G4-7	Nature of ownership and legal form	About us	32		Yes
G4-8	Markets served	About us	35		Yes
G4-9	Scale of the reporting organisation	Capital Highlights	10 to 13		Yes
G4-10	a. Total employees by employment contract and gender	Staff on contract is immaterial and hence was not reported.			Yes
	b. Total number of permanent employees by employment type and gender.	Management Discussion and Analysis	119 & 120		Yes
	c. Total workforce by employees, supervised workers and by gender	Based on nature of operations, supervised form of workers are immaterial.			Yes
	d. Total workforce by region and gender	Management Discussion and Analysis	119 & 120		Yes
	e. Whether substantial portion of work is done by self-employed or other outside parties other than employees.	Substantial portion of work is carried out by workers employed by the Company on a permanent basis.			Yes
	f. Significant variations in employment numbers	Based on the nature of business, there are no significant variations in employee numbers.			Yes
G4-11	Percentage of total employees covered by collective bargaining agreements	Management Discussion and Analysis	126		Yes
G4-12	Description of the organisation's supply chain	Management Discussion and Analysis	110		Yes
G4-13	Material changes regarding size, structure, ownership or supply chain	About us	36		Yes
G4-14	How organisation addresses precautionary approach or principle	Management Discussion and Analysis Risk Management Report	106,107 263		Yes
G4-15	Externally developed economic, environmental and social charters and principles or other initiatives to which the organisation subscribes or endorses	Management Discussion and Analysis	153 & 154		Yes
G4-16	Memberships in associations and national or international advocacy organisations in which the organisation holds position, participates in projects and committees, provides funding and views membership as strategic	Corporate Governance Report	187		Yes
G4-17	**Identified Material Aspects and Boundaries** (a.) List of entities included in the organisation's Consolidated Financial Statements (b.) Entities not covered in report pertaining to (a.) above	About us	6		Yes

G4 index	Description of Disclosure required	Disclosure given section/ remarks	Page number	If disclosure is omitted, reason for omission	Externally assured
G4-18	(a.) Process for defining the report content and the Aspect Boundaries	About us	40		Yes
	(b.) Approach to implementing the report principles for Defining Report Content	About us	44 to 47		Yes
G4-19	Identified Material Aspects, in the process for defining report content	About us	44 to 47		Yes
G4-20	For identified Material Aspect, the Aspect Boundary within the organisation	About us	44 to 47		Yes
G4-21	For identified Material Aspect, the Aspect Boundary outside the organisation	About us	44 to 47		Yes
G4-22	Effect of any restatement of information provided in previous reports with reason for such restatements	None material to report.			Yes
G4- 23	Significant changes from previous reporting periods in the scope and Aspect Boundaries	None material to report.			Yes
	Stakeholder Engagement				
G4-24	List of stakeholder groups engaged by the organization	About us	41 to 43		Yes
G4-25	Basis for identification and selection of stakeholders with whom to engage	About us	41 to 43		Yes
G4-26	» Approach to stakeholder engagement, including frequency of engagement by type and by stakeholder group;	About us	41 to 43		Yes
	» Indication of whether any of the engagements were undertaken specifically as part of the report preparation process	Majority of engagements were carried out in the normal course of business. Selectively, specific engagements were carried out with customers, employees, society etc. depending on organisational needs.			
G4-27	» Key topics and concerns raised through stakeholder engagement and how the organisation responded to those key topics and concerns » Stakeholder groups that relate to key topics and concerns	About us	41 to 43		Yes
	Report profile				
G4-28	Reporting period for information provided	1st April 2016 to 31st March 2017			Yes
G4-29	Date of most recent previous report	31st March 2016			Yes
G4-30	Reporting cycle	In annual cycle's			Yes
G4-31	Contact point for questions regarding the report or its contents	Overview section	8		Yes
G4-32	(a.) "In accordance" option chosen	Overview section	7		Yes
	(b.) GRI Content Index	Management Discussion and Analysis	158 to 169		Yes
	(c.) External Assurance Report	Management Discussion and Analysis	170		Yes
G4-33	Policy and current practice with regard to seeking external assurance for the report	External Assurance was sought from MI's External Auditors who are independent of the Company, its Board and shareholders.			Yes
		Overview section	8		Yes

GRI G4 Content Index : ‘In accordance ’ - Comprehensive

G4 index	Description of Disclosure required	Disclosure given section/ remarks	Page number	If disclosure is omitted, reason for omission	Externally assured
	Governance				
G4-34	**Governance structure and Composition** Governance structure including Committees under the highest governance body responsible for economic, social and environment decision-making	Corporate Governance Report	185, 186, 188 & 197		Yes
G4-35	The process for delegating authority for economic, environmental and social topics from the highest governance body to senior executives and other employees	Corporate Governance Report	186, 194		Yes
G4-36	Appointment of executive-level positions with responsibility for economic, environmental and social topics and reporting mechanism to highest governance body	Corporate Governance Report	186		Yes
G4-37	Processes for consultation between stakeholders and the highest governance body on economic, environmental and social topics	Corporate Governance Report	187		Yes
G4-38	Composition of highest governance body and its committees	Corporate governance report	185, 186, 188, 197 & 223		Yes
G4-39	Whether chair of the highest governance body is an executive officer	Corporate governance report	186 to 188		Yes
G4-40	The nomination and selection processes for the highest governance body and its committees and the criteria used for nominating and selecting highest governance body members	Corporate governance report	188		Yes
G4-41	Process adopted in ensuring conflicts of interest related to the highest governance body is avoided and managed and reported in related disclosures.	Corporate governance report Directors interest in contracts and related party notes to the accounts	188, 189, 221 & 236		Yes Yes
	Highest Governance Body’s Role in setting purpose, values and strategy				
G4-42	Roles of the highest governance body’s and senior executives in the development, approval and updating of the organisation’s purpose, value or mission statement, strategies, policies and goals related to economic, environmental and social impacts	Corporate governance report	185, 186, 194 & 217		Yes
	Highest Governance Body’s Competencies and Performance Evaluation				
G4-43	Measures taken to develop and enhance the highest governance body’s collective knowledge of economic, environmental and social topics.	Corporate governance report	195		Yes
G4-44	Process and actions taken in relation to the evaluation of the highest governance body’s performance with respect to governance of economic, environmental and social topics.	Corporate governance report	186 & 195		Yes

G4 index	Description of Disclosure required	Disclosure given section/ remarks	Page number	If disclosure is omitted, reason for omission	Externally assured
	Highest Governance Body's Role in Risk Management				
G4-45	Role of the highest governance body in the identification and management including implementation of due diligence processes in relation to economic, environmental and social impacts, risks and opportunities. A further level of stakeholder consultation is needed in this process.	Corporate governance report Risk Report	185, 186, 187 & 196 247		Yes Yes
G4-46	Role of the highest governance body's involved in reviewing the effectiveness of the organisation's risk management processes for economic, environmental and social topics.	Corporate governance report Risk Report	196 243, 244 & 247		Yes Yes
G4-47	Frequency of the highest governance body's in reviewing of economic, environmental and social impacts, risks and opportunities	Corporate governance report Risk Report	185, 186, 188 & 196 244		Yes Yes
	Highest Governance Body's Role in Sustainability Reporting				
G4-48	Highest committee or position that formally reviews and approves the organisation's sustainability report	Overview Corporate governance report	8 186		Yes Yes
	Highest Governance Body's Role in evaluating Economic, Environment and Social Performance				
G4-49	Process adopted to communicate critical concerns to the highest governance body	Corporate governance report	185 & 186		Yes
G4-50	Nature and total number of critical concerns communicated to the highest governance body and the mechanisms used to address and resolve them.	Corporate governance report	185, 186 & 187		Yes
	Remuneration and Incentives				
G4-51	Remuneration policies including performance criteria for the highest governance body and senior executives in relation to economic, environmental and social objectives	Corporate governance report	195		Yes
G4-52	Process of determining remuneration including whether remuneration consultants are independent	Corporate governance report	195		Yes Yes
G4-53	Views of stakeholders in relation to remuneration including results of votes on related policies and proposals, if applicable	Corporate governance report	195		Yes
G4-54	Ratio of the annual total compensation for the highest paid individual in each country to the median annual total compensation for all employees in the same country	Corporate governance report	195 and 126		Yes

GRI G4 Content Index :
'In accordance ' - Comprehensive

G4 index	Description of Disclosure required	Disclosure given section/ remarks	Page number	If disclosure is omitted, reason for omission	Externally assured
G4-55	Ratio of percentage increase in annual total compensation for the highest paid individual in each country to the median percentage increase in annual total compensation for all employees in the same country	Corporate governance report	195 and 126		Yes
	Ethics and Integrity				
G4-56	Organisation's values, principles,standards and norms of behavior adopted	About us Corporate governance report	33 214		Yes
G4-57	Internal and external mechanisms for seeking advice on ethical and lawful behavior and matters related to organisational integrity, such as helplines or advice lines	Corporate governance report	195, 221 & 233		Yes
G4-58	Internal and external mechanisms for reporting concerns about unethical or unlawful behavior and matters related to organisation's integrity including whistle-blowing mechanisms or hotlines	Corporate governance report	233		Yes

Specific Standard Disclosure :

G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page number	If disclosure is omitted, reason for omission	Externally assured
	Category : Economic				
	Economic Performance				
G4-DMA	Management Approach	Management Discussion and Analysis	88		Yes
	» Financial services sector specific DMA on economic performance	Management Discussion and Analysis	88		Yes
G4-EC1	» Direct economic value generated, distributed and retained	Management Discussion and Analysis	88 to 90 & 92		Yes
	» Economic performance financial services sector specific disclosure	Management Discussion and Analysis	88 & 89		Yes
G4-EC2	Financial implications and other risks and opportunities for the organisation's activities due to climate change	Management Discussion and Analysis	136		Yes
G4-EC3	Coverage of Defined Benefit Plan obligations	The Financial Statements	301		Yes
G4-EC4	Financial assistance received from the Government	Management Discussion and Analysis	109		Yes
	Market Presence				
G4-DMA	Management Approach	Management Discussion and Analysis	35 & 93		Yes
G4-EC5	Ratios of standard entry level wage by gender compared to local minimum wage at significant locations of operation	Management Discussion and Analysis	125		Yes
G4-EC6	Proportion of senior management personnel hired from local communities at significant locations of operation	Management Discussion and Analysis	120		Yes
	Indirect Economic Impacts				
G4-DMA	Management Approach	Management Discussion and Analysis	92		Yes
G4-EC7	Development and impact of infrastructure investments and service supported	Management Discussion and Analysis	92 & 93		Yes
G4-EC8	Significant indirect economic impacts, including impact extent	Management Discussion and Analysis	93		Yes
	Procurement practices				
G4-DMA	Management Approach	Management Discussion and Analysis	110		Yes
G4-EC9	Proportion of spending on local suppliers at significant location of operations	Management Discussion and Analysis	110		Yes

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G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page number	If disclosure is omitted, reason for omission	Externally assured
	Category : Environmental				
G4 -DMA	***Materials***	Management Discussion and Analysis	137		Yes
G4-EN1	Materials used by weight or volume	Management Discussion and Analysis	137 & 138		Yes
G4-EN2	Percentage of materials used that are recycled input materials	Management Discussion and Analysis	137 & 138		Yes
	Energy				
G4 -DMA	Management Approach	Management Discussion and Analysis	138 & 139		Yes
G4-EN3	Energy consumption within the organization	Management Discussion and Analysis	138 & 139		Yes
G4-EN4	Energy consumption outside the organisation	Management Discussion and Analysis	139		Yes
G4-EN5	Energy intensity	Management Discussion and Analysis	139		Yes
G4–EN6	Reduction in energy consumption	Management Discussion and Analysis	139		Yes
G4–EN7	Reductions in energy requirements of products and services	Management Discussion and Analysis	136		Yes
	Water				
G4-DMA	Management Approach	Management Discussion and Analysis	140		Yes
G4-EN8	Total water withdrawal by source	Management Discussion and Analysis	140		Yes
G4–EN9	Water sources significantly affected by withdrawal of water	Management Discussion and Analysis	140		Yes
G4–EN10	Percentage and total volume of water recycled and reused	Management Discussion and Analysis	140		Yes
	Bio-Diversity				
G4-DMA	Management Approach	Management Discussion and Analysis	143		Yes
G4 –EN11	Operational sites owned, leased, managed in protected areas and areas of high bio-diversity value outside protected areas.	Management Discussion and Analysis	143		Yes
G4 –EN12	Description of significant impacts of activities, products and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas	Management Discussion and Analysis	143		Yes
G4 –EN13	Habitats protected or restored	Management Discussion and Analysis	143		Yes
G4 –EN14	Total number of IUCN red listed species and national conservative list species with habitats in areas affected by operations by level of extinction risk	Management Discussion and Analysis	143		Yes
	Emissions				
G4 -DMA	Management Approach	Management Discussion and Analysis	140 & 141		Yes
G4–EN15	» Direct Greenhouse Gas (GHG) Emissions (scope 1) » Sector Specific additional disclosure	Management Discussion and Analysis	140 & 141		Yes Yes
G4 –EN16	» Energy indirect GHG emissions (scope 2) » Sector Specific additional disclosure	Management Discussion and Analysis	140 & 141		Yes Yes
G4 –EN17	» Other indirect GHG emissions (scope 3) » Sector Specific additional disclosure	Management Discussion and Analysis	140 & 141		Yes Yes
G4 –EN18	GHG emissions intensity	Management Discussion and Analysis	140 & 141		Yes
G4 –EN19	Reduction of GHG emissions	Management Discussion and Analysis	140 & 141		Yes
G4 –EN20	Emissions of ozone depleting substances (ODS)	Management Discussion and Analysis	140 & 141		Yes
G4 –EN21	NOx, Sox, and other significant air emissions	Management Discussion and Analysis	140 & 141		Yes

G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page number	If disclosure is omitted, reason for omission	Externally assured
	Effluents and Waste				
G4 -DMA	Management Approach	Management Discussion and Analysis	140		Yes
G4-EN 22	Total water discharge by quality and destination	Management Discussion and Analysis	140		Yes
G4-EN 23	» Total weight of waste by type and disposal method, reuse, recycling, composting » Financial services sector specific disclosure	Management Discussion and Analysis	140		Yes Yes
G4-EN 24	Total number and volume of significant spills	Management Discussion and Analysis	140		Yes
G4-EN 25	Weight of transported, imported, exported, or treated waste deemed hazardous under the terms of the BASEL Convention and percentage of transported waste shipped internationally	Management Discussion and Analysis	140		Yes
G4-EN 26	Identity, size, protected status, and biodiversity value of water bodies and related habitats significantly effected by the organisation's discharge of water and runoff	Management Discussion and Analysis	140		Yes
	Products and services				
G4 -DMA	Management Approach	Management Discussion and Analysis	136 & 137		Yes
G4-EN27	Extent of impact mitigation of environmental impacts of products and services	Management Discussion and Analysis	136 & 137		Yes
G4-EN 28	Percentage of products sold and their packaging materials that are reclaimed by category	Management Discussion and Analysis	136 & 137		Yes
	Compliance				
G4 -DMA	Management Approach	Management Discussion and Analysis	143		Yes
G4-EN29	Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with environmental laws and regulations	Management Discussion and Analysis	143		Yes
	Transport				
G4 -DMA	Management Approach	Management Discussion and Analysis	139		Yes
G4-EN30	Impacts of transporting products and other goods and materials for operations and transporting members of the workforce	Management Discussion and Analysis	139		Yes
	Overall				
G4-DMA	Management Approach	Management Discussion and Analysis	142 & 143		Yes
G4 – EN 31	Total environmental protection expenditures and investments by type	Management Discussion and Analysis	143		Yes
	Supplier Environment Assessment				
G4 -DMA	Management Approach	Management Discussion and Analysis	143		Yes
G4 – EN 32	Percentage of new suppliers that were screened using environmental criteria	Management Discussion and Analysis	143		Yes
G4 – EN 33	Significant actual and potential negative environmental impacts in the supply chain and actions taken	Management Discussion and Analysis	143		Yes
	Environment Grievance Mechanisms				
G4-DMA	Management Approach	Management Discussion and Analysis	143		Yes
G4-EN34	Number of grievances about environmental impacts filed, addressed and resolved through formal grievance mechanisms	Management Discussion and Analysis	143		Yes

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G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page Number	If disclosure is omitted, reason for omission	Externally assured
G4 -DMA	**Category : Social** **Subcategory – Labour practices and decent work** ***Employment***				
G4 -DMA	Management Approach	Management Discussion and Analysis	116		Yes
G4- LA1	Total number and rate of new employee hires and employee turnover by age group, gender, and region	Management Discussion and Analysis	119 to 121		Yes
G4- LA2	Benefits provided to full-time employees that are not provided to temporary or part-time employees, by significant locations of operation	Management Discussion and Analysis	126		Yes
G4- LA3	Return to work and retention rates after parental leave, by gender	Management Discussion and Analysis	124		Yes
	Labour/Management Relations				
G4-DMA	Management Approach	Management Discussion and Analysis	126 & 127		Yes
G4- LA4	Minimum notice periods regarding operational changes, including whether it is specified in collective agreements	Management Discussion and Analysis	126 & 127		Yes
	Occupational Health and safety				
G4-DMA	Management Approach	Management Discussion and Analysis	124		Yes
	» Sector specific additional DMA	Management Discussion and Analysis	124		Yes
G4- LA5	Percentage of total workforce represented in formal joint management worker health and safety committees that help monitor and advise on occupational health and safety programs	Management Discussion and Analysis	124		Yes
G4-LA 6	Type of injury and rates of injury, occupational diseases, lost days absenteeism and total number of work-related fatalities, by region and by gender	Management Discussion and Analysis	124		Yes
G4-LA 7	Workers with high incidence or high risk of diseases related to their occupation	Management Discussion and Analysis	124		Yes
G4-LA 8	Health and safety topics covered in formal agreements with trade unions	Management Discussion and Analysis	124		Yes
	Training and Education				
G4-DMA	Management Approach	Management Discussion and Analysis	121 & 122		Yes
G4- LA 9	Average hours of training by gender and by employee category undertaken during the reporting period by employees	Management Discussion and Analysis	122 & 123		Yes
G4- LA 10	Programs for skills management and lifelong learning that support the continued employability and managing career endings	Management Discussion and Analysis	123		Yes
G4- LA 11	Percentage of employees receiving regular performance and career development reviews by gender and employee category	Management Discussion and Analysis	123		Yes
	Diversity and equal opportunity				
G4- DMA	Management Approach	Management Discussion and Analysis	118 to 120		Yes
G4- LA 12	Composition of governance bodies and breakdown of employees category according to gender, age group, minority group membership and other indicators of diversity	Management Discussion and Analysis Corporate governance report	118 to 120, 187 & 190		Yes

G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page Number	If disclosure is omitted, reason for omission	Externally assured
	Equal remuneration for men and women				
G4- DMA	Management Approach	Management Discussion and Analysis	125 & 126		Yes
G4- LA 13	Ratio of basic salary and remuneration of women to men by employee category, by significant locations of operation	Management Discussion and Analysis	125 & 126		Yes
	Labour Practices and Grievance Mechanisms				
G4-DMA	Management Approach	Management Discussion and Analysis	125		Yes
G4- LA 16	Number of grievances about labour practices filed, addressed and resolved through formal grievance mechanisms	Management Discussion and Analysis	125		Yes
	Subcategory – Human rights				
	Investment				
G4 -DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR1	Total number and percentage of significant investment agreements and contracts that include human rights clauses or that underwent human rights screening	Management Discussion and Analysis	127		Yes
G4-HR2	Total hours of employee training on human rights policies	Management Discussion and Analysis	127		Yes
	Non-Discrimination				
G4 -DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR3	Total number of incidents of discrimination and corrective actions taken	Management Discussion and Analysis	127		Yes
	Child labour				
G4-DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR5	Operations and significant suppliers identified as having significant risk of forced or compulsory labour and measures taken to contribute to the effective abolition of child labour	Management Discussion and Analysis	127		Yes
	Forced or Compulsory labour				
G4-DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR6	Operations and suppliers identified as having significant risk for incidents of forced or compulsory labour and measures to contribute to the elimination of all forms of forced or compulsory labour	Management Discussion and Analysis	127		Yes
	Security Practices				
G4-DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR7	Percentage of security personnel trained in the organisation's human rights policies or procedures that are relevant to operations	Management Discussion and Analysis	127		Yes
	Assessment				
G4-DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR9	Total number and percentage of operations that have been subject to human rights reviews or impact assessments	Management Discussion and Analysis	127		Yes
	Human Rights Grievance mechanism				
G4-DMA	Management Approach	Management Discussion and Analysis	127		Yes
G4-HR12	Number of grievances about human rights impacts filed, addressed and resolved through formal grievance mechanisms	Management Discussion and Analysis	127		Yes

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G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page Number	If disclosure is omitted, reason for omission	Externally assured
	Subcategory – Society				
	Local communities				
G4 -DMA	Management Approach	Management Discussion and Analysis	144 to 146		Yes
G4-SO1	Percentage of operations with implemented local community engagement, impact assessments and development programs	Management Discussion and Analysis	144 to 147, 149 to 152		Yes
G4-SO2	Operations with significant actual and potential negative impacts on local communities	Management Discussion and Analysis	144 to 146		Yes
	Sector Specific Indicators				
G4-FS13	Access points in low-populated or economically disadvantaged areas by type	Management Discussion and Analysis	144 to 147		Yes
G4-FS14	Initiatives to improve access to financial services for disadvantaged people	Management Discussion and Analysis	144 to 147		Yes
	Anti-Corruption				
G4-DMA	Management Approach	Management Discussion and Analysis	147 & 148		Yes
G4-SO3	Total number and percentage of operations assessed for risks related to corruption and the significant risks identified	Management Discussion and Analysis	147 & 148		Yes
G4-SO4	Communication and training on anti-corruption policies and procedures	Management Discussion and Analysis	147 & 148		Yes
G4-SO5	Confirmed incidents of corruption and actions taken	Management Discussion and Analysis	148		Yes
	Compliance				
G4-DMA	Management Approach	Management Discussion and Analysis	148		Yes
G4-SO8	Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with laws and regulations	Management Discussion and Analysis	148		Yes
	Grievance mechanism for impacts on society				
G4-DMA	Management Approach	Management Discussion and Analysis	148		Yes
G4-SO11	Number of grievances about impacts on society filed, addressed and resolved through formal grievance mechanisms	Management Discussion and Analysis	148		Yes
	Subcategory – Product Responsibility				
G4 -DMA	Customer health and safety	Management Discussion and Analysis	107		Yes
G4-PR1	Percentage of significant products and service categories for which health and safety impacts are assessed for improvement	Management Discussion and Analysis	107		Yes
G4-PR2	Total number of incidents of non-compliance with regulations and voluntary codes concerning the health and safety impacts of products and services during their life cycle, by type of outcomes	Management Discussion and Analysis	107		Yes
	Product and Service Labeling				
G4 -DMA	Management Approach » Sector specific DMA	Management Discussion and Analysis Management Discussion and Analysis	107 97		Yes Yes
G4-PR3	Type of product and service information required by the organisation's procedures for product and service information and labeling, and percentage of significant products and service categories subject to such information requirements	Management Discussion and Analysis	107		Yes

G4 index	Material Aspects and related specific standard disclosures, DMA/ Indicator	Disclosure / Reference to disclosure	Page Number	If disclosure is omitted, reason for omission	Externally assured
G4-PR4	Total number of incidents of non-compliance with regulations and voluntary codes concerning product and service information and labeling by type of outcomes	Management Discussion and Analysis	107		Yes
G4-PR5	Results of surveys measuring customer satisfaction	Management Discussion and Analysis	107		Yes
	Marketing communications				
G4-DMA	Management Approach	Management Discussion and Analysis	106 & 107		Yes
G4- PR6	Sale of banned or disputed products	Management Discussion and Analysis	106 & 107		Yes
G4-PR7	Total number of incidents of non-compliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion and sponsorship by type of outcomes	Management Discussion and Analysis	107		Yes
	Customer privacy				
G4-DMA	Management Approach	Management Discussion and Analysis	107		Yes
G4-PR8	Total number of substantiated complaints regarding breaches of customer privacy and losses of customer data	Management Discussion and Analysis	107		Yes
	Compliance				
G4-DMA	Management Approach	Management Discussion and Analysis	107		Yes
G4-PR9	Monetary value of significant fines for non-compliance with laws and regulations concerning the provision and use of products and services	Management Discussion and Analysis	107		Yes
	Product portfolio				
G4-DMA	Management Approach » Sector specific DMA	Management Discussion and Analysis Management Discussion and Analysis	97 97		Yes Yes
G4-FS6	***Sector Specific Indicators*** Percentage of the portfolio for business lines by specific region, size and by sector	Management Discussion and Analysis	87, 92 & 93		Yes
G4-FS7	Monetary value of products and services designed to deliver a specific social benefit for each business line broken down by purpose	Management Discussion and Analysis	146 & 147		Yes
G4-FS8	Monetary value of products and services designed to deliver a specific environmental benefit for each business line broken down by purpose	Management Discussion and Analysis	136		Yes
	Stand alone disclosure on product responsibility: » Audit Management Approach	Management Discussion and Analysis	106		Yes

External Assurance Report Sustainability

BDO

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E-mail : bdopartners@bdo.lk
Website : www.bdo.lk

Chartered Accountants
"Charter House"
65/2, Sir Chittampalam A Gardiner Mawatha
Colombo 02
Sri Lanka

INDEPENDENT ASSURANCE REPORT TO THE STAKEHOLDERS OF MERCANTILE INVESTMENTS AND FINANCE PLC ON THE SUSTAINABILITY REPORT – 2017

Introduction And Scope of The Engagement

The management of Mercantile Investments and Finance PLC ("the company") engaged us to provide an independent assurance on the following elements of the Sustainability Report 2017 ("the Report").

- Reasonable assurance on the information on financial performance as specified on pages 89-90 of the Report.
- Limited assurance on key performance indicators and other information presented in the Report prepared in accordance with the requirements of Global Reporting Initiative G4 in accordance with – comprehensive guideline.

Responsibility of The Management On The Report

The Management of the company is responsible for the preparation and presentation of the Report in accordance with the company's sustainability practices and policies which are derived from Global Reporting Initiatives GRI (G4) in accordance with – Comprehensive Sustainability Reporting Guidelines. These responsibilities include among other things, identification of stakeholders and material issues, determining the sustainable performance criteria for reporting and establishing appropriate processes and internal control systems to measure and report the sustainability performance criteria.

Our Responsibility

Our responsibility is to perform a reasonable and limited assurance engagement and express conclusions based on the work performed in accordance with Sri Lanka Standard on Assurance Engagements (SLSAE 3000): 'Assurance Engagements other than Audits or Reviews of Historical Financial Information', issued by the Institute of Chartered Accountants of Sri Lanka ('CASL').

Reasonable assurance is a high level of assurance. However, reasonable assurance is not an absolute level of assurance because there are inherent limitations of assurance engagement.

A limited assurance engagement is substantially less in scope than a reasonable assurance engagement and consequently does not enable to obtain assurance that we would become aware of all significant matters that might be identified in a reasonable assurance engagement.

This Report is made solely to the company in accordance with our engagement letter dated 24th April, 2017. We disclaim any assumption of responsibility for any reliance on this Report to any person other than the company or for any purpose other than that for which it was prepared. In conducting our engagement, we have complied with the independence requirements of the Code of Ethics for professional Accountants issued by the CASL.

Assurance Procedures Carried Out

Financial Information

We reconciled the information on financial performance as reported on pages 89-90 of the Report with the audited financial statements of the company for the years ended 31st March, 2017 and 2016.

Key Performance Indicators

We reviewed the reliability of the data/information on Key Performance Indicators for the year ended 31st March, 2017 based on reviews of:

- the systems used to generate, aggregate and report these information;
- the information reported by the relevant business units to corporate level;
- the information validation processes at corporate and business level;
- the information trends in discussions with management; and
- the calculation performed by the company on a sample basis through recalculation.

Other Information

We planned and performed following assurance procedures on other information presented in the Report:

- Inquiring relevant company's personnel to understand the process for collection, analysis, aggregation and presentation of information in the Report.
- Reviewing the system used to generate, aggregate and report the information in the Report.
- Interviewing the senior management and relevant staff at corporate level and selected business unit level and obtained the evidence concerning sustainability strategy and policies for material issues and implementation of those across operation of the company.
- Reviewing and validating the information contained in the Report.
- Reading the information presented in the Report to determine whether that information is in line with our overall knowledge of, and experience with, sustainability performance of the company.
- Comparison of the content of the report against the criteria for a Global Reporting Initiatives G4 in accordance with – Comprehensive Sustainability Reporting Guideline.

Conclusion

Based on the procedures performed, as described above, we conclude that:

- The information on financial performance as specified on pages 89-90 of the Report is properly derived from the audited financial statements of the company for the years ended 31st March, 2017 and 2016.
- Nothing has come to our attention that causes us to believe that key performance indicators and other information presented in the Report are not presented, in all material respects, in accordance with the company's sustainability practices and policies which are derived from GRI (G4) in accordance with - Comprehensive Sustainability Reporting Guidelines.

BDO Partners

CHARTERED ACCOUNTANTS
Colombo
12th September, 2017
HA/um

Stewardship

sol•id

adjective

1. *firm and stable in shape*
2. *strongly built or made of strong materials*

Synonyms

1. well built, sound. 2. substantial, strong. 3. sturdy, durable.

Stewardship

Board of Directors 174 - 177
Corporate Management Team 178 - 181
Corporate Governance Report 182 - 242
Risk Management Report of The Company 243 -267

Board of Directors

Saroja Hemakumar Jayawickrema Weerasuriya

Chairman (Independent Non-Executive)

Gerard George Ondaatjie

Managing Director (Executive)

Pathiranage Mahes Amarasekara

Deputy Managing Director (Executive)

Shermal Hemaka Jayasuriya

Finance Director (Executive)

Angeline Myrese Ondaatjie

Director (Executive)

Travice John Ondaatjie

Director (Executive)

Punyakanthi Tikiri Kumari Navaratne

Director (Independent Non-Executive)

Nawagamuwage Hasantha Viraj Perera

Director (Non-Executive)

Singappuli Mudiyanselage Susantha Sanjaya Bandara

Director (Independent Non-Executive)

Pathmanathan Cumarasamy Guhashanka

Director (Independent Non-Executive)

Board of Directors

Saroja Hemakumar Jayawickrema Weerasuriya

BSc (Lond.), MICE. FIE (SL),
FSSE (SL), FIPM (SL) C.Eng.

Chairman
Independent Non-Executive
Appointed 26 January 2011
Areas of expertise and contribution:
Civil Engineering, Project Management, Tourism, Financial Services and Insurance Sector

Directorships, senior positions held and memberships:
Director of Kognoscenti (Pvt) Limited and Ceylinco Insurance PLC
Proprietor of Saro Weerasuriya Associates

Gerard George Ondaatjie

B.Sc. (Accountancy)
(Arizona State University – USA)

Managing Director
Executive
Appointed 2 December 1993
477,213 Voting shares
Areas of expertise and contribution:
Financial Services, Tourism and Trading Sector

Directorships, senior positions held and memberships:
Chairman and Managing Director of Fair View Hotel (Pvt) Limited
Chairman of Nilaveli Hotels (Pvt) Limited
Executive Deputy Chairman of Nilaveli Beach Hotels (Pvt) Limited
Managing Director of Mercantile Fortunes (Pvt) Limited, The Nuwara Eliya Hotels Co. PLC and Mercantile Orient (Pvt) Limited
Director of Tangerine Beach Hotels PLC, Royal Palms Beach Hotels PLC,
Security Ceylon (Pvt) Limited, Tangerine Tours (Pvt) Limited,
Global Films Limited, International Fortunes (Pvt) Ltd

Pathiranage Mahes Amarasekara

Deputy Managing Director
Executive
Appointed 18 December 1995
Areas of expertise and contribution:
Financial Service Sector

Directorships, senior positions held and memberships:
Director of Security Ceylon (Pvt) Limited and Fair View Hotel (Pvt) Limited

Shermal Hemaka Jayasuriya

FCA, FCMA (UK), CGMA, FCMA (SL), MBA (Sri.J.)

Finance Director
Executive
Appointed 5 January 2001
Areas of expertise and contribution:
Financial Services, Insurance, Manufacturing and Trading sector

Directorships, senior positions held and memberships:
Director of Mercantile Fortunes (Pvt) Limited and Security Ceylon (Pvt) Limited
Director of The Finance Houses Association of Sri Lanka

Angeline Myrese Ondaatjie

MBA(University of Texas in Austin) USA, BSc (Massachusetts Institute of Technology USA)

Director
Executive
Appointed 20 January 1992
477,213 Voting shares
Areas of expertise and contribution:
Financial Services, Tourism and Manufacturing sectors

Directorships, senior positions held and memberships:
Managing Director of Tangerine Tours (Pvt) Limited
Joint Managing Director of Tangerine Beach Hotels PLC, Royal Palms Beach Hotels PLC
Director of The Nuwara Eliya Hotels Co. PLC, Mercantile Fortunes (Pvt) Limited, Security Ceylon (Pvt) Limited, Nilaveli Beach Hotels (Pvt) Limited, Global Films Limited, International Fortunes (Pvt) Limited, Mercantile Orient (Pvt) Ltd, Fair View Hotel (Pvt) Limited, Nilaveli Hotels (Pvt) Limited.
Vice President of Tourist Hotels Association
Director of Sri Lanka Tourism Promotion Bureau
Serves on the Education Council of MIT

Travice John Ondaatjie

BSc (Arizona State University - USA)

Director
Executive
Appointed 13 July 1995
477,213 Voting shares
Areas of expertise and contribution:
Financial Services and Tourism sectors

Directorships, senior positions held and memberships:
Managing Director of Nilaveli Beach Hotels (Pvt) Limited, Nilaveli Hotels (Pvt) Limited
Director of Tangerine Beach Hotels PLC, Royal Palms Beach Hotels PLC, The Nuwara Eliya Hotels Co. PLC, Mercantile Fortunes (Pvt) Limited, Security Ceylon (Pvt) Limited, Fair View Hotel (Pvt) Limited, Tangerine Tours (Pvt) Limited, Global Films Limited, International Fortunes (Pvt) Limited, Mercantile Orient (Pvt) Limited

Punyakanthi Tikiri Kumari Navaratne

LLB (Col.), Attorney at Law

Director
Independent Non-Executive
Appointed 17 January 2012
Areas of expertise and contribution:
Legal & IT sectors

Directorships, senior positions held and memberships:
Vice President-Legal Affairs at WSO2 Lanka (Pvt) Limited
Colombo Agencies Ltd

Nawagamuwage Hasantha Viraj Perera

Diplomas in Business Management, Organizational Behaviour and HR Management

Director
Non-Executive
Appointed 9 February 2012
10,020 shares
Areas of expertise and contribution:
Legal, Financial Services, Tourism and Hotels Sector

Directorships, senior positions held and memberships:
Tangerine Beach Hotels PLC, Royal Palms Beach Hotels PLC, Blue Oceanic Beach Hotel Limited, Yala Safari Beach Hotels Limited, Yala Properties (Private) Limited, Southasia Economic and Trade Corporation (Private) Limited, Ceylon Electro Mechanical Services (Private) Limited, Desano Investments Limited, Tisara Hotels (Private) Limited, Thisara Investments (Pvt) Ltd and Koggala Beach Hotel (Private) Limited

Singappuli Mudiyanselage Susantha Sanjaya Bandara

FCA (SL), FAAT (SL), MBA (Col.), BSc.(Sri J.)

Director
Independent Non-Executive
Appointed 9 February 2012
Areas of expertise and contribution:
Accounting, Audit & Finance

Directorships, senior positions held and memberships:
Director of Nexia Management Services (Private) Limited & Nexia BPO (Private) Limited

Pathmanathan Cumarasamy Guhashanka

MBA (USA)

Director
Independent Non-Executive
Appointed 28 June 2013
Areas of expertise and contribution:
Automobile, Construction and Financial Services Sector

Directorships, senior positions held and memberships:
Group Director of Micro Holdings (Pte) Limited and its Subsidiaries
CEO of Micro Constructions (Pte) Limited
Director of Micro Cars Limited, Transmec International (Pte) Limited, Transmec Engineering (Pte) Limited & Euro Sports Auto Lanka (Pte) Limited, Fujitec Lanka (Pte) Ltd, Superlative Properties (Pvt) Ltd

Corporate Management Team

Dhanushka Fonseka

Director (Non-Board) – Credit & Marketing

Deva Anthony

General Manager - Finance

Ravi Ekanayake

General Manager – Workshop

Hirantha Pandithasekera

Assistant General Manager – Corporate Leasing

Dharshana Senerath

Assistant General Manager - Leasing

Lahiru Dayananda

Assistant General Manager – Credit & Marketing

Prasad Indika

Assistant General Manager - IT

Jayanka Kahawevithana

Assistant General Manager - Legal

Roshini Induruwage

Assistant General Manager – Deposits & Marketing

Asanthi Gunaratne

Assistant General Manager – Human Resources

Shehan Cooray

Assistant General Manager - Recoveries

Tharanga Deepal Peiris

Assistant General Manager - Microfinance

Sonali Pethiyagoda

Company Secretary

Prasad Wickramasinghe

Senior Manager – Payments & Cost Control

Chandana Nanayakkara

Senior Manager - Finance

Thamal De Silva

Senior Manager – Marketing And Communication

Avindra Wijesundara

Senior Manager – Credit Operations

Chaminda Paranayapa

Senior Manager – Insurance

Corporate Management Team

Wasantha Petikiri

Senior Manager – Legal

Dinesh Perera

Regional Manager – Leasing Negombo

Pubudu Dayaratne

Regional Manager

Nilusha Perera

Regional Manager

U M M K Bandara

Regional Manager

Dinesh Prabhath

Manager – Internal Audit

Shehan Sandanayaka

Manager – Risk & Compliance

Dhanushka Fonseka
Member of CIM, MBA (Wales)

Director (Non-Board) – Credit & Marketing
Areas of expertise and contribution:
19 years experience in the Financial Service sector
Directorships and memberships:
Director of Fair View Hotels
Member of Credit Committee

Deva Anthony
FCA, FCMA (UK), CGMA, FCMA (SL), ACIM

General Manager - Finance
Areas of expertise and contribution:
15 years experience in the Financial Service sector
6 years experience in audit and accounting

Ravi Ekanayake
Dipl. Engineering (UK)

General Manager – Workshop
Areas of expertise and contribution:
35 years experience in the automobile industry (In UK and Sri Lanka)
Directorships and memberships:
Director of Mercantile Fortunes (Pvt) Ltd

Hirantha Pandithasekera

Assistant General Manager – Corporate Leasing
Areas of expertise and contribution:
15 years experience in the Financial Service sector
2 years experience in the insurance field

Dharshana Senerath

Assistant General Manager - Leasing
Areas of expertise and contribution:
19 years experience in the Financial Service sector

Lahiru Dayananda

Assistant General Manager – Credit & Marketing
Areas of expertise and contribution:
17 years experience in the Financial Service sector

Prasad Indika
FBCS, Dip. (NIBM)

Assistant General Manager - IT
Areas of expertise and contribution:
14 years experience in the Financial Service sector

Jayanka Kahawevithana
LLB (Hons.), Attorney-at-law, Notary Public, Commissioner for Oaths

Assistant General Manager - Legal
Areas of expertise and contribution:
7 years experience in the Financial Service sector

Roshini Induruwage
MBA (Australia)

Assistant General Manager – Deposits & Marketing
Areas of expertise and contribution:
17 years experience in the Banking and Financial Service sector

Asanthi Gunaratne
LLM (London), Attorney-at-Law

Assistant General Manager – Human Resources
Areas of expertise and contribution:
10 years experience in Human Resources
5 years experience in legal field
2 years experience as a Company Secretary

Shehan Cooray

Assistant General Manager - Recoveries
Areas of expertise and contribution:
17 years experience in the Financial Service sector
Over one and half years experience in inbound sector

Tharanga Deepal Peiris
Dipl. Micro Finance (IBSL)

Assistant General Manager - Micro Finance
Areas of expertise and contribution:
16 years experience in the Financial Service sector

Sonali Pethiyagoda
ACIS (UK), ACCS

Company Secretary
Areas of expertise and contribution:
26 years experience in the Financial Service and tourism sector

Prasad Wickramasinghe
Diploma in taxation (CA Sri Lanka)

Senior Manager – Payments & Cost Control
Areas of expertise and contribution:
29 years experience in the Financial Service sector

Chandana Nanayakkara
ACA, ACMA(SL), CTA

Senior Manager - Finance
Areas of expertise and contribution:
12 years experience in the Financial Service sector
6 years experience in audit and assurance sector

Thamal De Silva

Senior Manager – Marketing And Communication
Areas of expertise and contribution:
21 years experience in Marketing

Avindra Wijesundara

Senior Manager – Credit Operations
Areas of expertise and contribution:
19 years experience in the Financial Service sector

Chaminda Paranayapa

Senior Manager – Insurance
Areas of expertise and contribution:
27 years experience in the Insurance Field

Wasantha Petikiri
LLB (Hons.), Attorney-at-Law, Notary Public and Commissioner for Oaths

Senior Manager – Legal
Areas of expertise and contribution:
12 years experience in the Financial Services Sector

Dinesh Perera
MBA (Australia) Member of MABE (UK)

Regional Manager – Leasing Negombo
Areas of expertise and contribution:
19 years experience in the Financial Service sector

Pubudu Dayaratne

Regional Manager
Areas of expertise and contribution:
14 years experience in the Financial Service sector

Nilusha Perera
MBA (UK)

Regional Manager
Areas of expertise and contribution:
10 years experience in the Financial Service sector

U M M K Bandara
Fellow member of SLICM, PGDip. Business Management (Colombo), BA (Colombo)

Regional Manager
Areas of expertise and contribution:
18 years experience in the Financial Service sector

Dinesh Prabhath
ACA, ACMA (UK), CGMA, B.Sc.(Acc.Sp) Sri Jayawardanapura

Manager – Internal Audit
Areas of expertise and contribution:
5 years experience in the Financial Service sector
3 years experience in audit and assurance sector

Shehan Sandanayaka
ACMA (UK), CGMA, CA. Passed Finalist

Manager – Risk & Compliance
Areas of expertise and contribution:
5 years experience in the Accounting & Financial Service sector
4 years experience in audit and assurance

Corporate Governance Report

Chairman's Statement

At Mercantile Investments and Finance PLC (MI), we believe that good governance is crucial to the soundness and long term sustainability of our business. Driven by this belief, we continue to work towards building a robust and meaningful corporate governance framework that would spearhead progress across all aspects of our business. Finance companies should ensure that there is a strong governance framework within the organization in order to secure the interest of all its stakeholders. The extensive efforts undertaken by the Central Bank of Sri Lanka in strengthening the governance practices of the finance companies in the recent decade has further stabilized and solidified the LFC sector. Finance companies are now more resilient to external shocks and have a prudent governance system than in the past.

How We Govern Our Business at MI

MI's Board comprises of professional and qualified individuals who challenge, motivate and guide the business aligned with the Company's vision. They actively participate at meetings and continue to provide invaluable advice for the betterment of the Company. The Board is collectively responsible to all stakeholders for the sustainable achievement of MI's strategic objectives. In this context, the Board remains committed to maintain the highest standards of corporate governance and most importantly, to embed these standards consistently at all levels of the business.

In doing so, based on MI's effective governance framework, the Board provides necessary guidance to the Corporate Management to ensure the efficient use of resources, effective internal control procedures and a proactive risk management mechanism are instilled, in line with the Company's strategic priorities. The Board is also accountable for promoting a transparent reporting mechanism that will present a fair, balanced and understandable assessment of MI's position and prospects.

As part of this overall commitment, the Board has appointed several Sub-Committees to assist the Board in the discharge of its duties, roles and responsibilities for all Sub-Committees clearly defined and a Chairperson of each Sub-Committee assigned with the duty of providing feedback to the Board. The Board and Sub-Committees convene regular meetings to discuss matters of relevance, including MI's performance, credit quality, asset and liability management, risk management, strategy and compliance.

To achieve the desired objectives, reporting structures have been clearly defined allocation responsibilities related to diverse aspects of the finance business. The Board requires all employees of MI to adhere to high standards of ethics and business integrity, in discharging their duties, acting within the said structures and framework.

Strengthening Corporate Governance

In the year under review, MI revised the Board approved MI Anti-Money Laundering Policy document, in order to be compliant with the FIU Gazette that was released in 2016. The Board spent a significant proportion of its time streamlining and strengthening processes, to further support good governance.

As another major initiative, MI formed a high calibre IT Steering Committee, whose first task was to oversee the upcoming implementation of the core system. As a base of standardizing operational activities across our building brand network, steps were also taken to issue more detailed operational instructions by way of manuals. Of course, Financial Year 2016/17 was certainly another commendable year, where we initiated a stream of other measures also, to improve governance practices, which is summarized on page 183 in this supplement.

As in previous years, all the Sub-Committees functioned effectively as directed by the regulator, and I would like to take this opportunity to thank all the heads of the Sub-Committees for assisting me on our journey towards achieving the goals set at the beginning of the year. This year's Corporate Governance Report provides extensive disclosures about the organization's Board governance, corporate governance framework and performance governance practices in enhancing our six capitals business model.

Future Of Governance

The future will remain challenging as the markets move ahead with rapid developments. In order to cater to such developments, LFC sector will have to be more vigilant and aggressive in its strategy, whilst keeping impeccable performance standards through sound governance practices. Increasing rules and regulations will safeguard LFCs from external shocks and, most of all, the financial system. MI through its effective governance framework will be able to manage future challenges with confidence.

As the Chairman, I re-affirm the commitment of the Board of Directors and all company personnel in complying with the applicable regulatory and statutory requirements, to discharge their duties in accordance with the policies, procedures and standards of MI.

Saro Weerasuriya
Chairman

12th September 2017

Governance at Mercantile Investments & Finance PLC

Governance Actions 2016/17

- Issue of the revised Anti-Money Laundering Policy document to comply with FIU Gazette 2016.
- Formation of the IT Steering Committee and outlining of the Terms of Reference for the Committee.
- More detailed self-assessment criteria of the Board of Directors.
- Increased Internal Audit scope and coverage.

Governance Objectives

- To carry out business operations based on the governing philosophy of prudence and in keeping with best practice, to safeguard the assets of the Company, the investments of depositors and interests of key stakeholders.
- Ethical and compliant corporate behaviour to minimize reputational risk and safeguard the Company's Brand.

Governance Goals 2020

- Strengthen corporate planning and strategy process with greater involvement and periodic oversight of the Board to set and realign performance with targets.
- Improve the quality, relevance and timeliness of corporate information provided to the Board.
- Expand External and Internal Audit and Compliance coverage.

The Board has unanimously embraced the rules and regulations of the applicable governance frameworks as a compliance requisite and also to ensure that high standards are maintained in respect of good corporate governance. In order to be compliant with the numerous external regulations that are in force, the management conformed to all internal policies approved by the Board as follows;

Key Internal Regulations	Key External Regulations
Articles of Association	Finance Business Act No. 42 of 2011
Terms of Reference for Committees	Securities and Exchange Commission of Sri Lanka (SEC) Act No. 36 of 1987 (as amended)
Code of Business Conduct and Ethics	Code of Best Practice on Corporate Governance issued jointly by Institute of Chartered Accountants of Sri Lanka (ICASL) and SEC
Human Resource hand book	Finance Companies (Corporate Governance) Directions issued by CBSL
Communication Policy	Listing Rules of Colombo Stock Exchange(CSE)
Anti-money laundering/ KYC Policy	Companies Act No. 07 of 2007
Internal Control Processes and Procedures	Sri Lanka Deposit Insurance Scheme Regulations and Circulars
Whistle Blower Policy	Financial Transaction Reporting Act No. 06 of 2006 (FIU)
Departmental Procedure Manuals	Know Your Customer (KYC) and Customer Due Diligence (CDD) Rules
Liquidity Risk Management Policy	GRI Guidelines on Sustainability
Branch Compliance Checklist	Carbon Disclosure

Corporate Governance Report

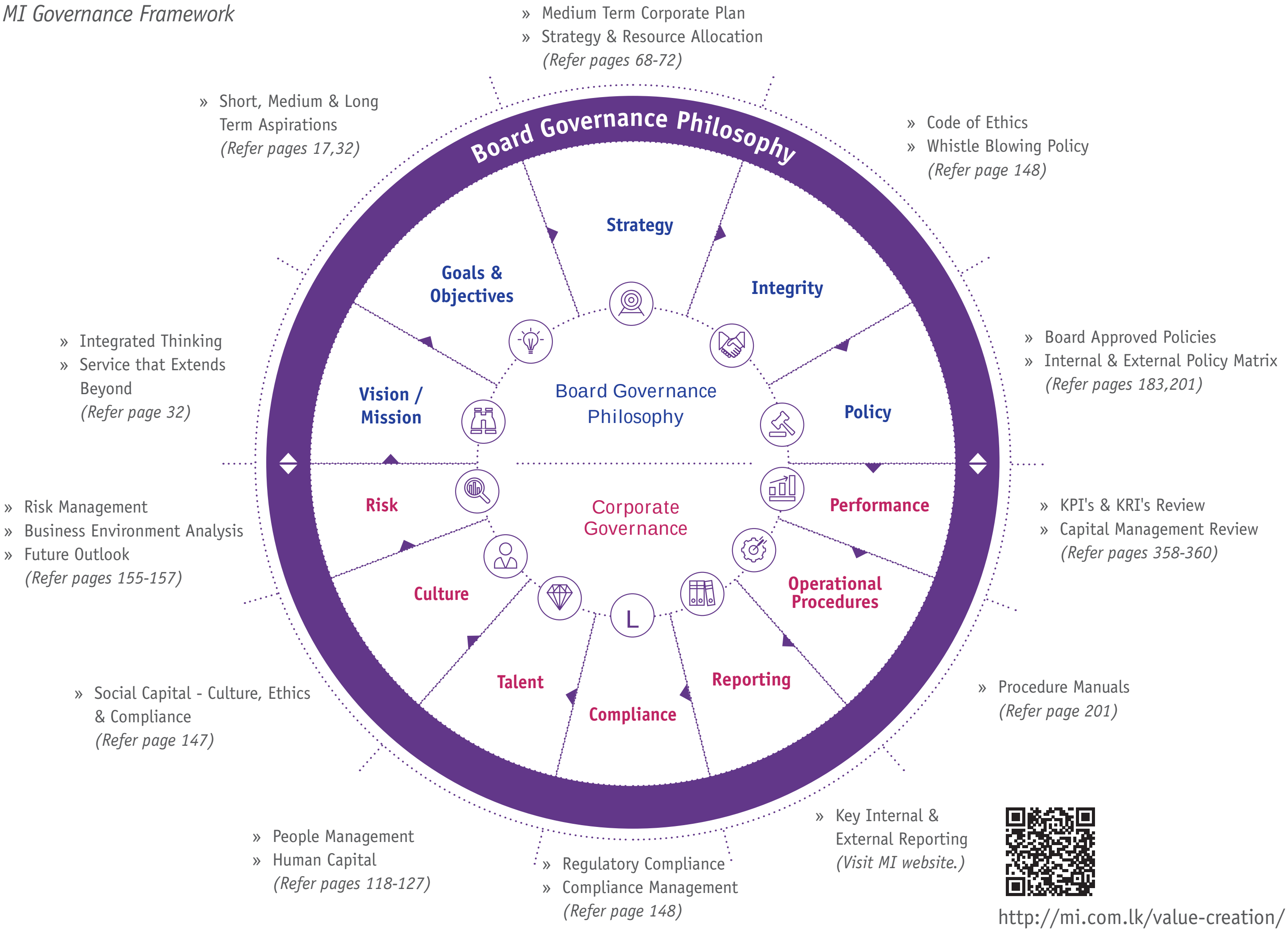
Based on the mandate given to the Integrated Risk Management Committee (IRMC), the area of compliance risk management was closely monitored by the committee including effectiveness of the Compliance Officer's (CO) role. During the Financial Year 2016/17, no material breaches have been identified that require separate disclosure.

The Board confirms that Mercantile Investments and Finance PLC is a going concern as indicated in the 2016/17 Annual Financial Statements and in the Annual Report of the Board of Directors. Accordingly the Annual Financial Statements and Interim Accounts have been prepared on the basis that the Company is a going concern.

Governance Framework

We govern the affairs of the Company using a governance framework that is comprehensive in meeting with requirements of the regulatory landscape and business objective of delivering sustainable value to all our stakeholders. The governance framework in place is structured and institutionalized across all levels of the Company through our strong corporate values, our culture, corporate policies and procedures and our overarching philosophy of prudence applied in the way we do business. The governance framework is continuously evolving in keeping abreast with the advancement in technology which is driving new ways of doing business and bringing with it a wide ranging set of regulatory compliance requirements in addition to the existing regulations and directives. Its design supports effective decision making and aides the provision of oversight and monitoring of compliance and performance in respect of all our key stakeholders. The governance framework for us is a collection of ideas, plans, people, processes, systems and assurance, that management has institutionalized in governing the daily affairs of the Company as depicted below.

MI Governance Framework



- » Medium Term Corporate Plan
- » Strategy & Resource Allocation
(Refer pages 68-72)

- » Code of Ethics
- » Whistle Blowing Policy
(Refer page 148)

- » Board Approved Policies
- » Internal & External Policy Matrix
(Refer pages 183,201)

- » KPI's & KRI's Review
- » Capital Management Review
(Refer pages 358-360)

- » Procedure Manuals
(Refer page 201)

- » Key Internal & External Reporting
(Visit MI website.)

- » Regulatory Compliance
- » Compliance Management
(Refer page 148)

- » People Management
- » Human Capital
(Refer pages 118-127)

- » Social Capital - Culture, Ethics & Compliance
(Refer page 147)

- » Risk Management
- » Business Environment Analysis
- » Future Outlook
(Refer pages 155-157)

- » Integrated Thinking
- » Service that Extends Beyond
(Refer page 32)

- » Short, Medium & Long Term Aspirations
(Refer pages 17,32)

http://mi.com.lk/value-creation/governance-risk-management/

Board Governance Philosophy

The bed rock of our governance framework is our overarching philosophy of prudence which we apply in managing the affairs of our Company and is enshrined in our culture and work ethics. Our governance framework supports the entire value generating process and systems from ideation to value generation for our stakeholders. We believe in accountability and responsible stewardship in generating value and benefits from the six forms of capital and in safeguarding the rights of our stakeholders through sustainable growth and profitability. (Refer Company History and Style of Management on page 33).

The Board plays an active role in designing the governance framework by providing leadership in drafting the policies, procedures and setting limits for the various risks to ensure the framework is robust and effective in supporting the operations of the Company in an ever changing dynamic environment, in measuring and managing performance and bringing risk within tolerance. The Board also provides oversight through the Sub-Committees of the Board and delegated authority to the Managing Director in ensuring that the strategic direction of the Company stays on course, obtains external and internal assurance to ensure that the control environment is robust and effective and that the affairs of the Company are in compliance with all mandatory, regulatory and statutory requirements.

The top half of the framework above depicts areas where the Board's involvement and responsibility is extensive. In these areas, it is generally not considered adequate for the Board only to understand and monitor the Company's operating model; in addition, the Board will be expected to play a major role in developing the components and participating in associated activities. The bottom half of the framework efficiently combines with the top depicted areas where the Board's responsibility can be described more as an active monitor with greater delegation handed down to Sub-Committees and senior management as it involves more in day to day operations.

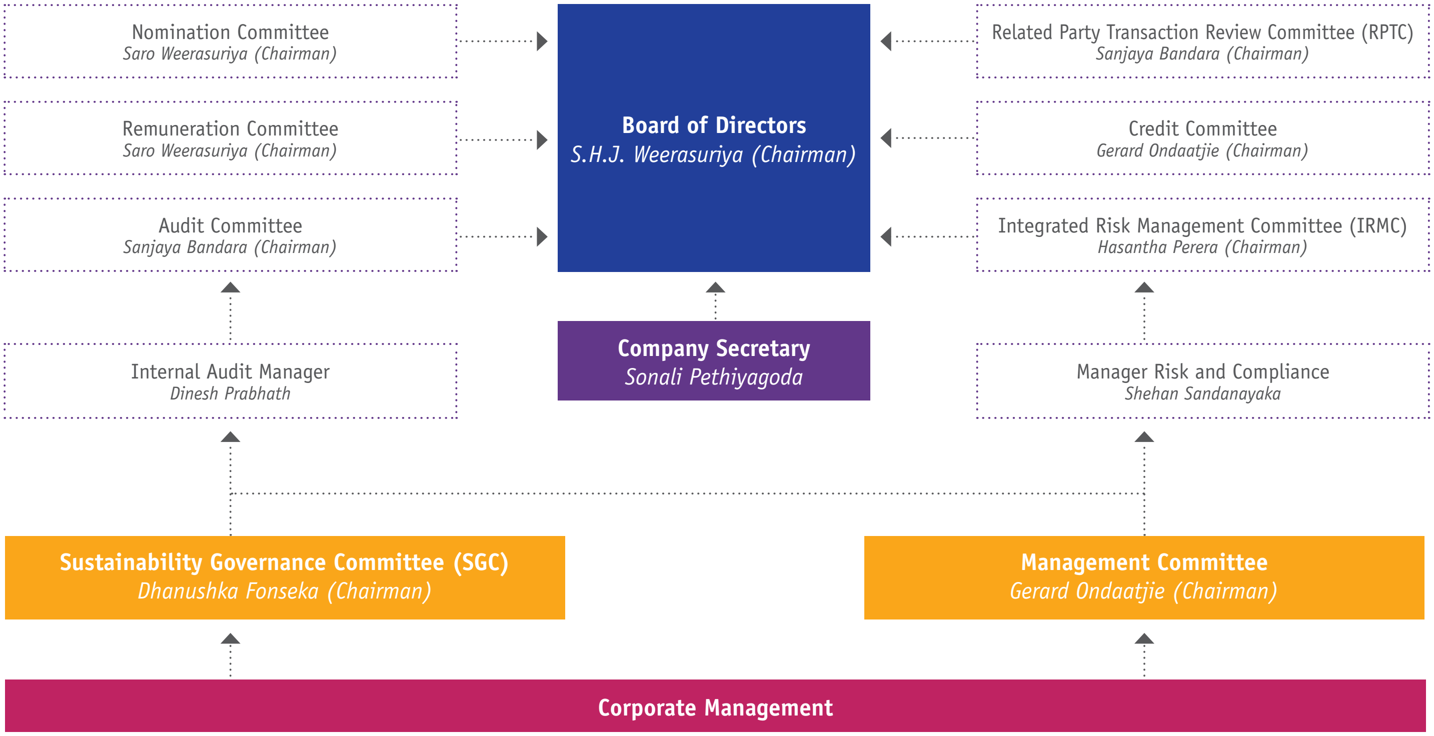
☑ *G4-38, 42, 45, 47, 49, 50*

MI Board's role in Governance

» The Board takes the lead in governing all matters associated with the Company's business activities and in doing so directing the Corporate Management through the Board appointed Sub-Committees with the collective insight and experience of the Board.

☑ *G4-34*

MI Governance Structure



Corporate Governance Report

- The Board focuses on driving a sustainable business, directing both the Corporate Management and the Sustainability Governance Committee (SGC) to generate sustainable economic, social and environmental value.
- The Board, through the Board appointed Sub-Committees and authority delegated to the Managing Director, provided necessary advice and guidance to the Corporate Management and the SGC for the achievement of sustainable objectives, and through its approval of the strategic plan and the monitoring of progress against the performance milestones. Executive Directors through formal Job Descriptions have been entrusted roles which require business specific goal attainment and broader economic, social and environmental sustainable target achievement.
- The Board's annual performance for the concluded financial period 2016/17 was reviewed by each Director by completing an evaluation checklist, which included a review of the economic, social and environmental effort.
- The organizational structure defines reporting lines for decision making, risk management, financial and regulatory reporting, public disclosures, and disaster recovery. The organizational structure enables the executive management to establish the independence and authority of the control functions of compliance, legal, finance, and audit.
- Define a process of overseeing the spectrum of risks across all regions, including strategic, operational, credit, liquidity, legal and compliance, and other risks.
- Maintain a governance structure that is understandable to internal employees and external stakeholders.

☑ *G4-34, 35, 36, 44, 48*

Governance Structure

The Board stands committed to the continuous creation of sustainable value to its stakeholders, and as part of its sustainability governance agenda has institutionalized an effective sustainability stewardship structure to expedite its plans effectively. Accordingly, the Board has entrusted the Sustainable Governance Committee to coordinate with key members of the Corporate Management to implement sustainability strategies, to fulfil the organisation's sustainability goals and aspirations. As a step towards effective sustainability governance, the Company starting from last financial year was able to incorporate its sustainability goals and develop suitable medium term strategies as part of its three year corporate plan. In keeping with these aspirations, both the Sustainable Governance Committee and the Corporate Management worked closely during the last two years to successfully launch the plans and create the required sustainable value from various perspectives.

Each Executive Director appraises the Board on the business related functional performance and status. The Finance Director/Chief Financial Officer, through the Manager Risk and Compliance continued to appraise the IRMC of SGC's sustainability efforts.

☑ *G4-38, 42, 45, 47, 49, 50*

Board oversight and responsibilities

The Board exercises oversight across the organization through the Board appointed committees and the Management Committee headed by the Managing Director which ranges from strategy formulation, financial decision making, risk review and regulatory compliance. In this regard, our governance framework assists the Board to:

- Determine the composition of the Board to ensure that the Board is equipped with the requisite knowledge, skills, competencies and experience necessitated to govern and provide guidance to the Company on matters of strategic importance and compliance by maintaining a mix of skills and experience among its members and maintaining the required balance between the number of Executive and Non-Executive Independent Directors in maintaining its independence and objectivity.
- Engage Management in evaluating the information provided to the Board on a broad range of strategic issues and objectives in exercising governance and oversight on matters of strategic importance and risk management.
- Draft the requisite policies and procedures that form an integral part of the governance framework.
- Scrutinize and evaluate the various activities of the control environment institutionalized across the Company to assess the suitability, relevance and effectiveness in supporting the current business landscape, and support Management in its efforts to improve performance and conformance with the multitude of regulatory and statutory requirements.

☑ *G4-39*

Chairman's Role at MI Board

The Chairman, who is an Independent Non-Executive Director, heads the Board and is entrusted to independently direct the affairs of the Board in collaboration with the other Board Directors, in guiding the Company towards achieving its sustainability agenda and long term business plans. (Refer to the Chairman's role, duties and responsibilities stated in page 203 in this report)

- *Remuneration*
- *Related Party Transaction Review*
- *Nomination*
- *Integrated Risk Management*
- *Audit*
- *Credit*

✓ *G4-LA12*

Total Numbers of Papers approved in 2016/17

» Submitted	*109*
» Approved	*74*
» Tabled	*35*

✓ *G4-LA12*

As at 31st March 2017

Gender

» Male	*8*
» Female	*2*

Age

» 45-50	*2*
» 50-55	*5*
» 55-60	*1*
» 60-65	*1*
» >65	*1*

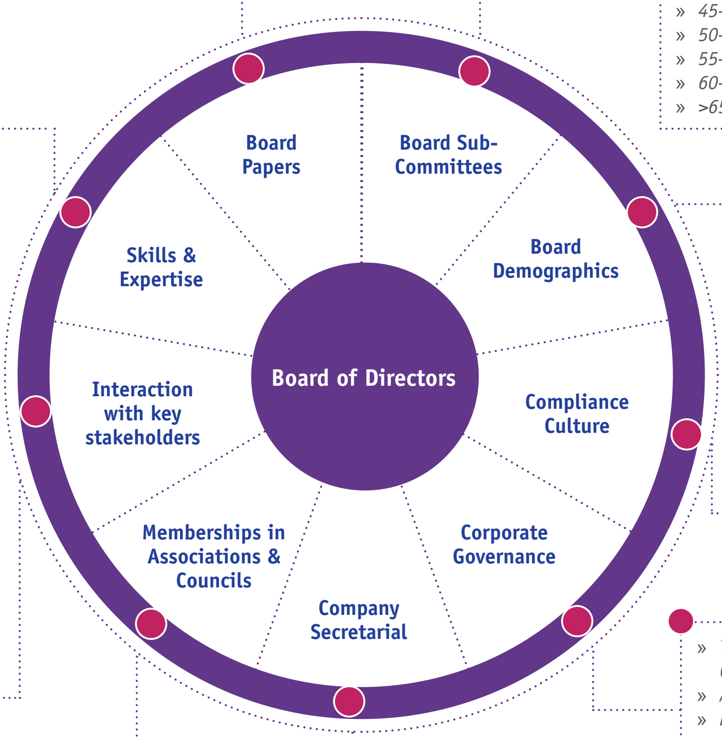
Category

» Executive	*5*
» Independent	*4*
» Non –Executive	*1*

Length of Service (years)

» 3-6	*4*
» 6-9	*1*
» >9	*5*

» Accounting & Auditing	*1*
» Financial Services	*6*
» Business Administration	*6*
» Trading	*2*
» Tourism	*3*
» Recoveries	*1*
» Insurance	*1*
» Manufacturing	*2*
» Legal Affairs	*2*
» Human Resource	*2*
» Engineering and Project Management	*1*



In a business environment where reputational threats lurk around every corner, a strong culture of ethics and compliance is the foundation of a robust governance program. At MI, our Board of Directors strongly advocate a culture of compliance that cascades down the organisational hierarchy.

✓ *G4-37, 45*

Shareholders;
- *at AGM*
- *through Mail*
- *by Appointment*
- *"feedback form" of the Annual Report*

Employees;
- *"Open Door Policy"*
- *Staff meetings*
- *Weekly corporate review meetings*
- *Board meeting & periodic and ad hoc meetings*

Other Stakeholders;
- *Ex. Dir. with MI customers, suppliers, lenders*
- *MD through the SGC engaged with communities*

- *The roles of the Independent Chairman and the CEO are separate*
- *Availability of a strong code of ethics*
- *Minimise the conflicts of interest of the directors*

✓ *G4-16*

- *Member of the Finance Houses Association of Sri Lanka*
- *Member of the Leasing Association of Sri Lanka*
- *Member of Ceylon Chamber of Commerce*
- *Member of the Integrated Reporting Council of Sri Lanka*

The Company Secretary is responsible for the efficient administration, particularly with regard to ensuring compliance with statutory and regulatory requirements and for ensuring that decisions of the Board of Directors are documented and implemented.

Corporate Governance Report

☑ G4-34, 38, 47

BOARD MEETINGS

The Company holds Board meetings at monthly intervals to ensure that the Board addresses all key issues on a timely basis, and directs the affairs of the Company, in a timely manner in meeting stakeholder expectations. Board meetings are scheduled in advance in consultation with the Directors to facilitate meaningful participation. The Company Secretary, with the guidance, and the overseeing by the Chairman, dispersed the agenda supported by related circulars/ information packs including the Notice of the Meeting, at least seven days prior to the meeting date to ensure that the members of the Board have sufficient time to go through the information provided. Directors are provided with comprehensive information in respect of agenda items in a timely manner, and they have the discretion to obtain independent advice whenever they require. The information circulated, included the monthly management accounts with key statistics and trends, together with information pertaining to other matters that are planned to be taken up for the meeting. The Directors were able to freely incorporate significant matters, proposals and statistics in the agenda, to be taken up at such meetings. Board papers passed on by the heads of divisions were taken up for discussion and approved during meetings. The Board being equally balanced possessed the necessary experience and qualifications to make informed decisions for the prudent running of the business.

An open dialogue between all Directors is encouraged by the Chairman at Board meetings. The Board members come well prepared and engage in meaningful discussions on key strategic issues relating to the Company. The CEO gives a complete and comprehensive update on the operations, financial and non-financial performance of the Company as well as on LFC sector trends and developments together with an update on any matters pertaining to the sustainability agenda of the Company. He also updates the Board on the risk dashboard of the Company and any changes to the risk profile of the Company. The Chairperson of each Board committee provides a detailed update on key matters discussed at the committee meetings together with the minutes of the subject committee meetings on demand. Regular updates on changes in accounting policy and statutory and/ or regulatory changes affecting the Leasing and Finance Industry, new tax implications, corporate governance initiatives and regulatory requirements which the Company needs to comply with, are brought up to the Board meeting by the relevant director with the functional expertise. In this manner, the Board is kept informed with new market developments and changes in the regulatory landscape and made aware of the possible implications to the Company on a timely basis.

(Refer to page 198 for information pertaining to Directors attendance at Board meetings for the financial year 2016/17)

☑ G4-39, 40, 41

Independent Selection of Board members

Through the Nominations Committee, there is continuous evaluation of the Board's capabilities skills and experience against evolving demands of the industry and the Company.

The Nominations committee recommends additional members to the Board, through a due assessment process that reviews the qualifications, capabilities, experience and skills of potential candidates. Information pertaining to the Nominations Committee is given on page 283.

To maintain independence and impartiality, the Chairman of the Board remains a Non-Executive Director.

In order that independence is maintained in handling related party transactions, the Board has established a "Related Party Transaction Committee" which functions independently from the Board. Information pertaining to the Boards Related Party Transaction Committee is given on page 285.

☑ G4-34

Board Sub-Committee Authorities and Responsibilities

The Board appointed subcommittee structure at MI defines the terms, responsibilities, reporting and escalation mechanisms, and ways in which the Board and Management will interact. The Board appointed subcommittee structure is outlined as follows,

- Include a committee charter that defines the committee's responsibilities and addresses linkages between the committee, the broader executive team, and the Board of Directors
- Define the scope of the committee outlining key responsibilities and areas of oversight, Composition of the committee and attendance records of members
- Report of the respective Committee
- Demonstrate methods of escalating and reporting significant matters to the appropriate person or committee

Table on Directorates/Equivalent Positions held by Directors as at 31st March 2017 ☑ G4-41

Name of the Director	No. of Directorates*	No. of Directorates**	Companies/Societies/Corporate Bodies including Associate Companies and Subsidiaries of the Finance Company																																	
			Mercantile Fortunes (Pvt) LTD	Nilaveli Beach Hotels (Pvt) LTD	Tangerine Beach Hotels PLC	Royal Palms Beach Hotels PLC	The Nuwara Eliya Hotels Company PLC	Tangerine Tours (Pvt) LTD	Security Ceylon (Pvt) LTD	Global Films LTD	International Fortunes (Pvt) LTD	Mercantile Orient (Pvt) LTD	Fair View Hotel (Pvt) LTD	Nilaveli Hotels (Pvt) LTD	The Light House Hotel PLC	Phoenix Industries LTD	Brushco (Pvt) LTD	Ceylinco Insurance PLC	Saro Weerasuriya Associates	Kognoscenti (Pvt) LTD	Blue Oceanic Beach Hotel Limited	Yala Safari Beach Hotel Limited	Yala Properties (Pvt) LTD	South Asia Economic and Trade Corporation (Pvt) LTD	Ceylon Electro Mechanical Services (Pvt) LTD	Desano Investments Limited	Tisara Hotels (Pvt) LTD	Koggala Beach Hotel (Pvt) LTD	WS02 Lanka (Pvt) LTD	B.R. De Silva & Co.	Nexia Management Services (Pvt) LTD	Nexia BPO (Pvt) LTD	Micro Holdings (Pvt) LTD	Micro Cars LTD	Micro Constructions (Pte) LTD	Transmec International (Pte) LTD	Transmec Engineering (Pte) LTD	Euro Sports Auto Lanka (Pte) LTD
Mr. S.H.J. Weerasuriya	3	1																*	*	*																		
Mr. G.G. Ondaatjie	12	3	*	*	*	*	*	*	*	*	*	*	*	*																								
Mr. P.M. Amarasekara	2	-							*				*																									
Ms. A.M. Ondaatjie	15	4	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*																					
Mr. T.J. Ondaatjie	11	3		*	*	*	*	*	*	*	*	*	*	*																								
Mr. S.H. Jayasuriya	2	-	*						*																													
Mr. N.H.V. Perera	10	2			*	*															*	*	*	*	*	*	*	*										
Ms. P.T.K. Navaratne	1	-																											*									
Mr. S.M.S.S. Bandara	3	-																												*	*	*						
Mr. P.C. Guhashanka	6	-																															*	*	*	*	*	*

No. of Directorates / Equivalent Positions Held in Other Companies/Societies/ Bodies Corporate

*** No. of Directorates/Equivalent Positions Held in Specified Business Entities*

Corporate Governance Report

Board Committee Overview

Board Committee	Audit Committee	Remuneration Committee	Integrated Risk Management Committee	Nomination Committee	Related Party Transaction Review Committee	Credit Committee
Members and 2016/17 Meeting Attendance	Independent Directors	Independent Directors	Independent Directors	Independent Directors	Independent Directors	Independent Directors
	S.M.S.S. Bandara 7/7	S.H.J. Weerasuriya 1/1	NIL	S.H.J. Weerasuriya 1/1	S.M.S.S. Bandara 4/4	NIL
	S.H.J. Weerasuriya 7/7	P.T.K. Navaratne 1/1		S.M.S.S. Bandara 1/1	S.H.J. Weerasuriya 4/4	
	Non-Executive Directors	Non-Executive Directors	Non-Executive Directors	Non-Executive Directors	Non-Executive Directors	Non-Executive Directors
	N.H.V. Perera 7/7	N.H.V. Perera 1/1	N.H.V. Perera 4/4	N.H.V. Perera 1/1	N.H.V. Perera 4/4	NIL
	Executive Directors	Executive Directors	Executive Directors	Executive Directors	Executive Directors	Executive Directors
	NIL	NIL	G.G. Ondaatjie 4/4	G.G. Ondaatjie 1/1	NIL	G.G. Ondaatjie 12/12
			S.H. Jayasuriya 4/4			P.M. Amarasekara 12/12
			P.M. Amarasekara 4/4			S.H. Jayasuriya 12/12
	Secretary	Secretary	Secretary	Secretary	Secretary	Secretary
	S. Pethiyagoda	S. Pethiyagoda	S. A. Sandanayaka	S. Pethiyagoda	S. Pethiyagoda	D. Fonseka
Key Responsibilities	Ensuring compliance to accounting standards and regulations specified by regulatory bodies including CBSL.	To identify and decide on Executive Director Remuneration levels and Non-Executive fees for the purpose of retaining high calibre individuals.	To oversee MI's risk management function and to identify risks, recommend solutions and report key risk concerns to the Board regularly.	Nominate members to MI's Board with the relevant knowledge, expertise and also identifying right calibre individuals for future succession.	To assist the Board in reviewing material – related party transactions carried out by MI and to provide feedback in the event of concerns.	Maintaining a sound credit review and disbursement and recovery process while approving credit as per entrusted authority.
	Ensuring compliance to disclosure requirements arising from accounting standards and regulations specified by regulatory bodies including CBSL.	Formulating remuneration strategy and policies.			Evaluation of significant acquisitions, disposals, investments, credit arrangements and related party transactions.	
	Providing oversight on the quality of financial reporting, ensuring relevant accounting policies are adopted.	Monitoring the implementation and effectiveness of such policies.				
	Evaluating the adequacy and effectiveness of the internal control system and setting up a process that provides continuous feedback.	Engaging where necessary with stakeholders on remuneration issues.				
	Dealing in matters related to the External Auditors and their nominations annually.					
	Following up on the observations and recommendations of Internal Auditors and reviewing their scope of work and engaging with External Auditors, Corporate Management to identify and resolve concerns.					

Board Committee	Audit Committee	Remuneration Committee	Integrated Risk Management Committee	Nomination Committee	Related Party Transaction Review Committee	Credit Committee
Actions For 2016/17	Reviewed the process of risk management to ensure the Company meets required risk management standards.	Approved annual increments for Executive Directors.	Determined the appropriate Risk Appetite and MI's level of exposure.	Recommended re-election of Directors retiring by rotation.	Reviewed and monitored related party transactions of MI.	Appraised existing lending policies and assessed credit risk evaluations of large lendings and high risk accounts including guarantors.
			Established a method for overseeing the overall risk management process of the Company.	Assessed the composition of the Board.	Formulated, revised and approved policies on related party transactions.	Reviewed existing and proposed exposure limits on customers against set parameters giving consideration to aspects such as lending growth, exposure values, risk levels of counterparties, overall sector exposure levels and demographic exposure levels.
	The Committee ensured that ICT system review is included into the annual audit process of the Company.		Identified risks and monitored the management of fundamental risks to reduce the likelihood of unwelcome surprises.		Advised management on reporting format to committee.	Recommended stringent action on problematic accounts in consultation with the legal division.
	Evaluated External Auditor's scope of work and its cost effectiveness with final results. Ensured that the required level of independence and objectivity was maintained when giving their audit opinion.		Approved major decisions affecting MI's risk profile and exposure.			Approved credit over a specified Board approved limit.
	Followed up on material observations highlighted in the letter to the Management by the External Auditor during their statutory audit of the previous period. The Committee invited the External Auditors to meet and discuss key matters.		Periodically reviewed MI's approach to risk management and approved changes/ improvements to key elements of its processes and procedures.			
	Reviewed the scope, functions and resources of the Internal Audit function and adequacy of audit programmes. The Committee approved audit programmes tabled by MI's own Internal Audit Division and outsourced part given to EY.					

Corporate Governance Report

Board Committee	**Audit Committee**	**Remuneration Committee**	**Integrated Risk Management Committee**	**Nomination Committee**	**Related Party Transaction Review Committee**	**Credit Committee**
	Reviewed integrity of the financial information generated by the Finance Department in consultation with the CFO. The Committee evaluated the accounting policies, accounting standards including IFRS new requirements adopted and other reporting requirements in accordance with the Companies Act, Finance Business Act and Colombo Stock Exchange rules.					
	Followed up with Corporate Management on material observations highlighted by Internal Auditors. At each meeting, Internal Auditors were requested to present key observations to the Committee, including due recommendations for rectification and to provide a status report on the remedial action taken by the Management.					
Board Paper Submission Status	Number of Board papers	Number of Board papers	Number of Board papers	Number of Board papers	Number of Board papers	Number of Board papers
	» Submitted 15	» Submitted 01	» Submitted 04	» Submitted 02	» Submitted 05	» Submitted 03
	» Approved 07	» Approved 01	» Approved 04	» Approved 02	» Approved 05	» Approved 0
	» Tabled 08	» Tabled 0	» Tabled 0	» Tabled 0	» Tabled 0	» Tabled 03

Management Committee

Board Committees	Management Committee	Assets and Liabilities Management Committee	Sustainability Governance Committee	IT Steering Committee
Members and 2016/17 Meeting Attendance	Executive Directors	Executive Directors	Executive Directors	Executive Directors
	G.G. Ondaatjie 12/12	G.G. Ondaatjie 12/12	Nil	S.H. Jayasuriya 2/2
	P.M. Amarasekara 12/12	P.M. Amarasekara 12/12		
	S.H. Jayasuriya 12/12	S.H. Jayasuriya 12/12		
		Travice Ondaatjie 12/12		
	Corporate Management Team	Corporate Management Team	Corporate Management Team	Corporate Management Team
	Secretary	Secretary	Secretary	Secretary
	S. A. Sandanayaka	S. A. Sandanayaka	S. De Silva	T. Zainudeen
Key Responsibilities	Reviewed management information on performance closely to identify early warning signs and to assess performance gaps so that prompt steps could be taken.	Overseeing, evaluating and making recommendations to the Board on broad Asset and Liability concerns, specifically focusing on liquidity and interest rate risks.	Guiding MI's sustainability value creation process and initiates with the Company making a thorough assessment of the prevailing internal and external considerations against MI's sustainability efforts, in relation to the key economic, social and environmental dimensions.	Take on responsibility for the project's feasibility, business plan and achievement of outcomes & ensure the project's scope aligns with the requirements of the stakeholder groups.
Actions For 2016/17	The Finance Division conducted weekly and monthly meetings and presented a stream of financial information in relation to lending, deposits, profitability, spread levels, market statistics and forecast.	Provided oversight on interest rate risks by monitoring related trends, impacts to net interest income margin changes and established effective counter measures.	Completion of the CSR projects that were ongoing and carried forward from the last financial year.	Formation of the Committee and outlining of the Terms of Reference for the committee, and received approval for the same from the Board of Directors.
	Financial and non-financial performance, actual versus past and against expected targets were revised and discussed.	Reviewed liquidity risks both short and long-term.	New appointments and re-appointments were carried out for the committee positions.	
	Monthly performance review with respective cluster AGMs, Regional Managers and other Key Officers.	Presented to the Board, concerns related to liquidity and interest rate risks.	Approved the list of CSR projects that are to be carried out during the 2016/17 financial year.	
		Recommended solutions for maturity mismatches in assets and liabilities.		
Board Paper Submission Status	Number of Committee papers	Number of Committee papers	Number of Committee papers	Number of Committee papers
	» Submitted 12	» Submitted 12	» Submitted 5	» Submitted 2
	» Approved 0	» Approved 0	» Approved 0	» Approved 0
	» Tabled 12	» Tabled 12	» Tabled 5	» Tabled 2

Corporate Governance Report

☑ G4-42

Strategic Planning

The Board approved the medium term three year corporate plan of the Company in 2015 which was developed with adequate insight, feedback, involvement and participation of the staff across the Company, the Corporate Management team and the participation of the Directors. The strategic plan encapsulated the Company's vision, mission and value system, and then defined clearly key corporate objectives which included the sustainability goals as well.

The Corporate Management and the SGC made evaluations on MI's sustainability efforts of the past, and were able to understand the resultant impacts to both the Company and its stakeholders.

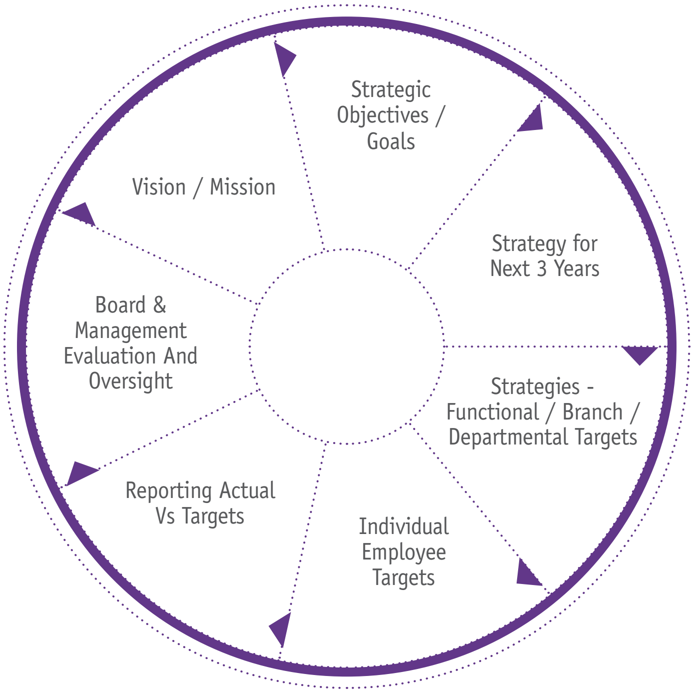
Based on the thorough analysis carried out on the economic, social and environmental impacts, the Company was able to develop a suitable medium term strategic plan with objectives towards sustainable growth and profitability and value creation to meet with stakeholder expectations.

The role of the Managing Director

The Managing Director is the Chief Executive Officer of the Company, and is delegated by the Board with the authority of detailed planning, the development of the corporate plan, implementation of strategic objectives, policies and procedures as approved by the Board and tasked with governance and compliance in accordance with governance and risk frameworks. He also has delegated limits of authority as prescribed by the Board to approve financial transactions, and enter into contracts on behalf of the Company. (Refer the CEO's role, duties and responsibilities stated in page 203 in this report)

☑ G4-42

Strategic Planning Process



☑ G4-35

The Corporate Management Committee's Role In Governance

- The Corporate Management Committee's role in governance primarily focuses on enhancing of investor wealth and meeting the stakeholder expectations, from a broader sustainability perspective bringing forth long-term economic value to the investors, the LFC sector and the economy as a whole.
- Along with this, the committee focuses on managing its people in an effective manner in order to excel in relationship management in terms of customers and staying compliant with regulatory requirements. Sustainability calls management to look beyond investors and consider all stakeholders.
- Development of the Company's leasing, lending business and deposit mobilization operation remained top priority.
- Respective Directors / GMs / AGMs and Managers were responsible to manage the performance of their staff in an effective manner to achieve targeted key operational goals and strive for sound financial results within the performance appraisal framework of the Company.
- Performance of each such strategic business units and support divisions were closely monitored by the Managing Director and other Executive Directors on behalf of the Board.
- During this period, the members of the Corporate Management team and the SGC were in parallel availed of the necessary resources, to pursue ways of identifying and enhancing sustainability value going beyond commercial boundaries. Their individual targets were aligned with corporate goals with targets also set to enhance sustainable practices of the Company over the previous year.

- In keeping to the strategic plan and the Company's business model, core divisional staff were requested to improve core business revenue to strive towards planned profitability targets, while in tandem the SGC pursued its responsibilities on creating greater social and environmental value by setting forth on worthy projects to be completed by the year end.

☑ G4-43,57

Employee Training on Regulations and Enriching Institutional Knowledge

Executive Directors, General Managers, Assistant General Managers and Senior Management have undergone the required technical training, apprising them of latest developments in the industry and regulatory landscape towards skill enhancement. This includes SGC members who have undergone external training on sustainability management.

The staff were also provided with different needs based training namely, internal training and induction programs conducted by in house resource personnel and external training conducted by industry specialists with expertise in the different disciplines. These trainings were carried out to ensure that our employees strictly adhere to rules and regulations applicable to LFC sector in Sri Lanka. Department wise training was conducted on a regular basis on regulations related to lending practices focusing on legal aspects, documentation and regulatory requirements. Selected employees were sent on special training conducted by the Central Bank, The Institute of Chartered Accountants, The Institute of Certified Management Accountants of Sri Lanka and Finance House Associations and other bodies that provide technical knowledge on prevailing regulations.

(Refer Human Capital on pages 116-127 for more details.)

☑ G4-44, 51, 52, 53, 54, 55

Performance Evaluation, Rewards and Recognition

- Performance of Executive-Board members including that of the Managing Director is assessed annually by the Remuneration Committee which functions as an independent Board appointed Sub-Committee.
- The Committee evaluates the performance of the Executive Directors and decides their remuneration levels, while also deciding on the Non-Executive Director fees based on the level of expertise and the contribution made by such Directors to the Board in terms of the time committed to activities of the Board.
- Details pertaining to the Remuneration Committee's composition and its delegated tasks are given on page 282.
- Any Changes to remuneration of the Corporate Management and other employees, is decided annually by the Managing Director together with the respective heads-of- divisions who are either Directors or senior officers of the Company.
- During this formal performance evaluation process, views of relevant employees, immediate supervisors and views of other functional heads were also taken into account.
- In deciding rewards such as bonuses, a similar formal evaluation was also carried out on a bi-annual basis for the employees.
- For the front-line business divisions, the employee evaluations presently focuses upon achievement of business targets and goals, by evaluating the actuals achieved against the individual targets.
- The support divisional staff's performance was assessed based on intangible requisites and other qualitative performance criteria.

Governance in Practice

The Board acknowledges the increase in responsibilities it now faces in overseeing the Management and providing oversight over the affairs of the Company, given the diverse stakeholder expectations, constantly changing regulatory landscape and complex business environment surrounding the LFC industry. The Board and its committees have a greater role to play in overseeing the affairs of the Company which includes oversight over wide ranging strategic issues that are constantly changing due to the dynamism of the industry and the increase in regulations that are being introduced due to digital disruption to the existing ways of doing business and automation and digitization of payment modes. In like manner, the Management and its committees are tasked with devoting more time to matters pertaining to governance and compliance in addition to managing the risk profile of the Company. The Board and the Management rely on expert opinion as and when required in arriving at informed decisions and obtain the assurance of both internal and external auditors on the effectiveness of the control environment and status on compliance with all applicable laws, statutory requirements and regulations including the accuracy of the financial reporting and compliance with the applicable accounting standards.

Hence, the governance and risk frameworks are constantly reviewed and amended to reflect the dynamism, complexity and compliance requirements of the industry while remaining institutionalized in the minds of the staff. Compliance and conformance form the main pillars of the overarching philosophy of prudence which has become a way of life, with accountability and responsibility continuing to shape our

Corporate Governance Report

culture that is built on trust, integrity and professionalism as intended by our founders. The governance framework is therefore a working document and provides the required clarity and understanding to the Directors and staff in governance roles in executing their duties with integrity.

Enhancing the Oversight Function

Strengthening of the Internal Audit Function

The addition of five new branches to the branch network demanded more heads to support the Internal Audit function, and as such four new recruitments were made. The internal audit function is been handled by both the Internal Audit Department as well as by Ernst & Young Advisory Services (Pvt) Limited. The review of the compliance status at Head Office and at branch level, in relation to laid down procedures and prevailing regulations, are the main focus areas of the Company's internal audit function. The Audit Committee provided oversight over both teams of internal and outsourced auditors and reviewed their findings in respect of weaknesses in the control environment, in the design of controls, and effectiveness of all manual and automated controls in the processes in scope. The Audit Committee also reviewed the feedback on the accuracy and completeness of the financial reporting and gaps in compliance along with the management actions towards re-mediation of the issues and gaps noted.

☑ *G4-45, 46, 47*

Strengthening The Risk Management Process

In order to strengthen the risk management process, the Company took a number of new initiatives for the financial year with oversight executed by the Manager – Risk and Compliance. (Refer the Risk Management Report from pages 243 to 267 for a comprehensive overview of MI's Risk Management process.)

Strengthening the Compliance Function

Due to the ever-increasing regulations from various regulatory authorities of the LFC sector, the Manager – Risk and Compliance who also functions as the Compliance Officer (CO) of the Company, is entrusted to oversee the level of compliance by the Company with the various regulatory and statutory directives, rules and regulations. The compliance status on CBSL regulations and guidelines are submitted to the Board on a monthly basis by the Manager – Risk and Compliance, from last financial year, and the Board was appraised on a monthly basis on MI's level of compliance to CBSL regulations.

The Company's Compliance Status to Key Corporate Governance Best Practices/Regulations

In order to reflect the extent of our compliance with the applicable statutory and regulatory compliance frameworks and best practices on corporate governance, four separate statements have been provided to illustrate the level of conformity with prevailing regulations and best practices on corporate governance.

Part one provides disclosure on the Company's level of conformity with the recommended Code of Best Practice on Corporate Governance, issued to public companies jointly by the Securities and Exchange Commission of Sri Lanka (SECSL) and The Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka) issued in September 2013.

Part two provides disclosure on the Company's level of compliance with the Direction issued on Corporate Governance to Finance Companies by the Central Bank of Sri Lanka, under Direction No. 03 of 2008 and amendments issued under Direction No. 04 of 2008 and Direction No. 06 of 2013.

Part three provides disclosure on the Company's level of compliance with sections 7.6 and 7.10 of the Listing Rules of the Colombo Stock Exchange (CSE) on Corporate Governance.

Part four provides disclosure on the Company's level of compliance with the rules and guidelines issued by the Central Bank of Sri Lanka to the LFC sector.

Mercantile Investments and Finance PLC's adherence with the Code of Best Practice on Corporate Governance Issued Jointly by The Institute Of Chartered Accountants of Sri Lanka and The Securities and Exchange Commission of Sri Lanka ("CODE")

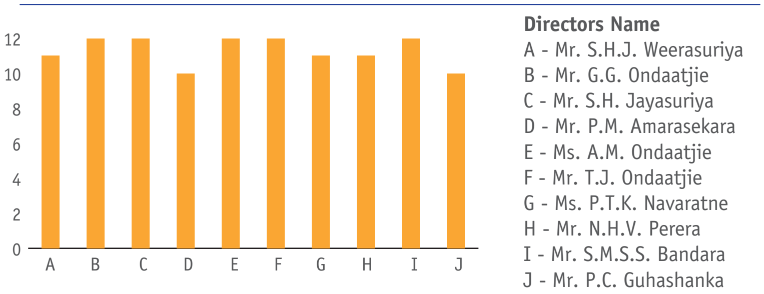
☑ *G4-34, 38*

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
Section 1 **The Company:** **A. Directors** **A.1. The Board**	**Principle A.1**	Adopted	The leadership for the Company is provided by an effective Board of Directors that comprises of experienced individuals with diverse backgrounds and expertise. The profile of the Board members is provided on pages 176-177. The Board comprises of an Independent Non-Executive Chairman who heads the Board and is well supported by the Managing Director and other Directors reflecting a sound balance between Independent and Executive Directors.

MI Board Competency Matrix

	Name of Director									
	S. H. J. Weerasuriya	**G. G. Ondaatjie**	**P.M. Amarasekara**	**S. H. Jayasuriya**	**A. M. Ondaatjie**	**T. J. Ondaatjie**	**P. T.K. Navaratne**	**N. H. V. Perera**	**S.M. S. S. Bandara**	**P. C. Guhashanka**
Expertise										
Strategic Management	x	x	x	x	x	x			x	x
Legal			x				x	x		
Recoveries			x	x				x		
Human Resource Management	x	x		x	x	x	x	x		
Financial	x	x		x	x	x			x	
Fundraising				x						x
Public Relation	x	x	x	x	x	x	x	x		x
Governance	x	x		x				x	x	x
Risk Management	x	x		x		x	x	x		
Sector										
Corporate							x	x		x
Legal Enforcement			x				x	x		
Education									x	
Engineering	x									
Small Businesses			x	x						
Tourism and Hotels	x	x			x	x		x		
Automobile		x	x	x		x				x
Financial Services	x	x	x	x	x	x				
Auditing									x	
Qualities										
Strategic Thinker	x	x		x	x	x	x		x	x
Visionary	x	x	x	x	x	x	x			x
Analytical	x	x	x	x	x	x		x	x	x
Idea Generator	x	x	x	x	x	x	x			x
Able to deal with ambiguity	x	x		x	x			x	x	x
Networking	x	x	x	x	x	x	x			x

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
1. Board meetings	Code A. 1.1	Adopted	The Board met 12 times during the financial year (FY) 2016/17, at monthly intervals to review the performance of the Company. A formal notice of meeting along with an agenda was sent by the Company Secretary at least 7 days prior to the meeting, with all Directors expected to be present. There were no special Board meetings held during the FY 2016/17. Attendance at Board Meetings 
2. Board Responsibilities	Code A. 1.2	Adopted	The Board being the apex decision-making point in the Company's hierarchy, is responsible for setting the overall strategy, Risk Appetite and approves capital and operating plans presented by the Management, for the achievement of the objectives it has primarily set. Apart from providing leadership to the Corporate Management, in setting the short, medium and long-term strategic goals, the Board ensures adequate resources are available to meet these objectives.
» Formulation and implementation of a sound business strategy			The Board, along with the Senior Management formulates key strategies, having analysed both the external and internal environment of the Company and taking account of all stakeholder requirements in setting objectives that address the short, medium and long term goals of the Company. As part of the strategic planning process, a corporate plan is formulated every three years, incorporating measurable goals, strategic initiatives and key performance indicators. The Board delegates to the Management, the implementation of the strategic priorities and policies within the approved risk parameters. An effective 3 year strategic plan was formulated and approved by the Board for a three year period during the financial year 2015/16. The corporate plan along with corporate values and strategies were communicated to the management team via the strategic planning exercise and for its implementation under the oversight of the Board. The budget is approved annually and the achievement of the targets are set out therein. Actual performance against the plan is reviewed by the Executive Directors at periodic meetings with updates provided by the senior management. The Board has delegated authority to Board committees and enabled them to oversee specific responsibilities, in order to discharge its stewardship and fiduciary responsibilities in an effective and timely manner.
» The CEO and management team possess the skills, experience and knowledge to implement the strategy			The Managing Director (MD) / CEO and Corporate management possess the required knowledge and skill with widespread experience in the LFC sector in order to execute the strategic plan formulated and approved by the Board. Refer: Corporate Management Profiles on Page 181 for details of skills and experience of individual members of the Corporate Management.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
» Adoption of an effective CEO and senior management succession plan			Succession to the key managerial positions (KMP) primarily focuses on developing and grooming people internally so as to have adequate options available within the Company in formulating an effective succession plan for key management personnel. The Board approved succession plan as well as the organizational structure of the Company which facilitates this process.
» Effective systems to secure integrity of information, risk management and internal controls			A comprehensive set of Board approved internal control policies and procedures have been adopted by the Company and institutionalized as part of the overarching philosophy of prudence. The management engages the services of Ernst and Young Chartered Accountants to review the control environment of the Company in addition to the work carried out by the internal auditors of the Company. The Board of Directors have delegated the authority to the Audit Committee to undertake the detailed monitoring of the controls and to report to the Board on its findings on a periodic basis with necessary management follow up actions being initiated by the Audit Committee. The internal control framework ultimately aims to safeguard stakeholder and depositor's interest and this importantly involves shareholders' investment in the Company's assets which are safeguarded against unauthorized use and disposal. External Auditors have been appointed to obtain assurance on the integrity of the published information and Financial Statements of the Company which are used to make key decisions. The Board acknowledges its responsibility to ensure the reliability and integrity of information of the Company. The Integrated Risk Management Committee (IRMC) reviews the risk reports of the Company and takes prompt corrective actions to mitigate the negative effects of specific risks. Refer the Report by the Board on Internal Controls on page 286 of this Report.
» Compliance with laws, regulations and ethical standards			The Company's Compliance function headed by Manager for Risk and Compliance, who is also the Compliance Officer (CO) of the Company, is responsible for the monitoring and assessing the Company's compliance with applicable laws, regulations, regulatory guidelines, internal controls and approved policies in all areas of business operations. The CO independently reports to the IRMC on a quarterly basis on regulatory risk factors impacting the business with recommendations.
» All stakeholder interests are considered in corporate decisions			The Board approved "Communication Policy" of the Company has been developed to gather information about stakeholder expectations and to disseminate information back to key stakeholders to ensure those responsibilities to shareholders and other stakeholders are appropriately discharged in a timely manner. The two way communication policy is an effective mechanism, in order to gain a clear understanding of the latest developments in stakeholder interests. The information gathered is used in the strategic planning process in formulating the corporate plan and setting the corporate objectives and in drafting the sustainability agenda of the Company. Refer: Relationship Capital on pages 94 to 115 and Stakeholder Engagement on pages 41 to 43

Corporate Governance Report

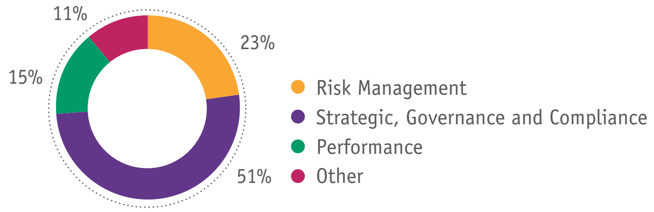
Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
» Sustainable business development in corporate strategy, decisions and activities			The Board has identified the importance of sustainable business development in formulating the corporate strategy, in its decision making process and activities of the Company. The corporate plan aims to create long term sustainable growth and profitability to enhance stakeholder value as a constant exercise. Bearing that in mind, a significant consideration is also given by the Board to discharge its corporate social responsibilities. The Company's integrated business model articulated on page 5 highlights how sustainable value is generated through the Company's business process.
» Ensuring the Company's values and standards are set with emphasis on adopting appropriate accounting policies and fostering compliance with financial regulations			In order to be in line with the new developments in the LFC sector and changing business requirements, the Company's accounting policies are reviewed annually by the Audit Committee. The Board ensures that the Financial Statements of the Company are prepared in accordance with the approved accounting policies, accounting standards and internal practices under the overarching philosophy of prudence and supported by the culture that fosters trust, integrity and ethical behaviour. Refer the Independent Auditors Report on page 288 which provides an opinion confirming that the Financial Statements prepared by the Company are in line with the applicable accounting standards and regulations and the report by the board on internal control over Financial Reporting appearing on page 286.
» Fulfilling other Board functions are vital given the scale, nature and complexity of the organisation			The Board stayed dedicated throughout the year in fulfilling its obligations towards all stakeholders and in providing the required oversight in monitoring the performance of the Company. The main focus areas were maintaining shareholder returns, maintaining credit ratings, institutionalizing sound corporate governance procedures and processes, reviewing compliance with all mandatory regulations and laws and ensuring that the identified risks were brought within tolerance. Key strategic financial decisions made by the Board related to funding, pricing, liquidity, cost benefit decisions on capital expenditure and reviewing of annual budgets. The Board also reviewed the existing policies of the Company and issued new policies in keeping with the current business requirements and regulatory landscape. The existing policies were amended where necessary.

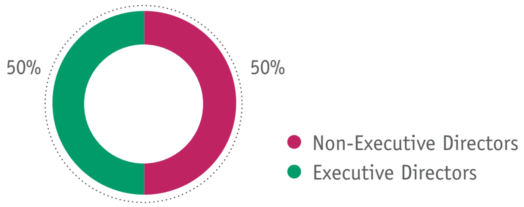
Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
			Key Policy Documents Issued Year

Document	Issued Year
Procedure Manual	2010
Business Continuity Plan	
Terms of Reference for the Integrated Risk Management Committee	2011
Terms of Reference for the Audit Committee	2011
Investment Policy	2011
Communication Policy	2011
Information Systems Security Policy	2012
Procedure to Seek Independent Professional Advice	2012
HR Policy	2013
Risk Management Policy	2013
Areas of Authority and Key Responsibilities of the Board	2013
Whistle Blowing and Corporate Fraud Policy	2013
Schedule of Matters Reserved for the Board (Revised)	2013
Nomination Committee Terms of Reference	2013
Credit Policy	2013
Recovery Policy	2013
Terms of Reference of Remuneration Committee	2014
Liquidity Risk Management Policy	2014
Remuneration Policy	2014
Terms of Reference for Remuneration Committee	2014
ICT Manual	2014
Liquidity Risk Management Policy	2014
Terms of Reference of Remuneration Committee	2014
Assets and Liabilities Committee (ALCO) Terms of Reference	2014
AML and CFT Policy	2015
Credit Committee Terms of Reference	2015
Related Party Terms of Reference	2016
IT Steering Committee Terms of Reference	2017

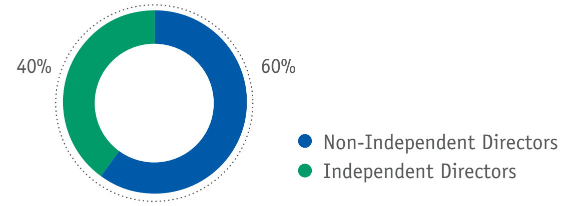
3. Compliance with laws and access to independent professional advice	Code- A. 1.3	Adopted	When considering the Company's compliance status with the regulatory and statutory requirements applicable to the Company, the Board collectively, as well as individually, has complied with all mandatory regulatory requirements. The Company has an established procedure set out in its Corporate Governance Charter that enables the individual Directors to seek professional independent advice on matters related to the exercising of their duties and responsibilities at the expense of the Company. However, no such advice was sought during the financial year 2016/17. Any instances of non-compliance are disclosed in the financial accounts sub note no 22, given on page 318 and note no. 53 given on page 354 . A compliance status update to applicable laws and regulations is provided on Page 276 by the Board of Directors.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
4. Company Secretary	Code – A. 1.4	Adopted	The Company Secretary, Mrs. S. Pethiyagoda, advises the Board and ensures that matters concerning the Companies Act, Board procedures and other applicable rules and regulations including Corporate Governance are duly followed. All Directors have access to the Company Secretary who is a qualified Chartered Secretary with over 20 years' experience. Her services were available to all the Directors, who needed support to ensure they received timely and accurate information to fulfil their duties. The appointment as well as the removal of the Company Secretary is a matter reserved for the decision by the Board. Refer page 181 for the profile of the Company Secretary.
5. Independent judgement	Code – A. 1.5	Adopted	The Board works as an effective and cohesive unit bringing independent and objective judgement, and scrutinising the recommendations/proposals made by heads of divisions and other Corporate Management Officers, on issues of strategy, performance, human resource practices, resource utilisation and business conduct. The majority of the Directors have been appointed to various Board Sub-Committees enabling them to exercise effective control over strategic, financial, HR, compliance and governance issues.
6. Dedication of adequate time and effort by the Board	Code- A. 1.6	Adopted	All Directors have been allocated sufficient time enabling them to discharge their duties and responsibilities effectively at Board and Board Sub-Committee meetings. The Board members have attended and participated in the majority of the meetings and have devoted adequate time. Information pertaining to Directors' attendance at Board meetings and Board Sub-Committee meetings are given on pages 190 and 198. Board Meeting Discussion Composition 
7. Training needs of Directors	Code – A. 1.7	Adopted	A comprehensive induction program is conducted for the new Directors, who are appointed to the Board. This program apprises them comprehensively on the values and the culture of the Company, business and operations and its strategies, policies, governance framework and processes and their responsibilities as a Director in terms of the applicable rules and regulations. Existing Directors are kept abreast of applicable legislation and regulations, changes to rules, standards and codes of conduct, as well as developments in the LFC sector that could impact the Company, and are encouraged by the Board to attend seminars and workshops covering technical and other current topics.
A.2 Chairman and Chief Executive Officer	**Principle- A.2**	Adopted	The roles of the Chairman and Managing Director/Chief Executive Officer have been segregated since 2012, ensuring a balance of power and authority in such a way that no individual has unfettered power over decision making. The Chairman leads the Board and is responsible for governance and the effective working of the Board. The Managing Director is responsible and accountable for day-to-day management of the affairs of the Company.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
8. Division of responsibility between the Chairperson and MD/CEO	Code – A. 2.1	Adopted	The roles of the Chairperson and Chief Executive have been kept separate. The Chairperson's main responsibility is to lead, direct and manage the Board ensuring that it operates effectively and fully discharges its legal and regulatory responsibilities in accordance with the requirements of the Companies Act No 7 of 2007 and as amended and other regulatory requirements. The Managing Director (MD) is in charge of the Company's chief executive role, managing the day-to-day operations of the Company. As part of his role, he leads the Corporate Management team in making and executing operational decisions within the limits of authority delegated to him by the Board. The MD is also responsible for recommending strategies to the Board.
A.3 Chairman's Role **G4 - 39**	**Principle – A.3**	Adopted	Mr. Saro Weerasuriya, the Chairman of the Board is an Independent Non–Executive Director. He leads and manages the Board, ensuring that it discharges its legal and regulatory responsibilities effectively, preserving order and facilitating the effective discharge of the Board function.
9. Chairperson's role in conducting Board proceedings	Code – A. 3.1	Adopted	The Chairman is responsible for preserving good corporate governance and leading the Board in an orderly and effective manner. In order to achieve the said objective, he handles specific duties which are critical in nature. Mr. Weerasuriya has to; » Maintain a high level of independence and impartiality in Board matters, and ensure the effectiveness of the Board. » Ensure adequate information is provided to the Directors on a timely basis. » Obtain advice from the Board members as required and ensure he addresses critical issues in a timely manner. » Prepare and circulate a formal agenda for the Board under his supervision. » Conduct the AGM and ensure active communication with the shareholders and key stakeholders.
A.4 Financial Acumen 10. Availability of sufficient financial acumen and knowledge within the Board	**Principle–A.4**	Adopted	Each Director of the Company brings a set of diverse skills and expertise to the boardroom, which ranges from accounting and auditing, financial services, insurance, business administration, engineering, recoveries, legal and human resources. In addition, the Company has engaged a highly qualified Finance Director to advise the Board on matters relating to finance, and who has demonstrated his competency by drawing from his vast experience in financial management, and his professional training. Refer Directors profile on page 176
A.5 Board Balance	**Principle – A.5**	Adopted	As clearly specified in the Finance Companies Corporate Governance Direction No. 03 of 2008 issued by CBSL, the Company maintained the required Board balance throughout the FY 2016/17, so that no individual or small group of individuals were able to dominate the Board's decision-making.
11. Presence of Non-Executive Directors	Code – A. 5.1	Adopted	During the year under review, the ratio of 50% between Executive and Non-Executive Directors was maintained throughout the period and is well above the minimum requirement prescribed by the code. Executive Vs. Non-Executive Directors 

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
12. Independent Directors	Code – A. 5.2	Adopted	Of the five Non-Executive Directors, four are independent, and the 80% ratio is maintained in terms of the criteria defined by CSE Rule 7.10.4 on corporate governance. The total Board position of Independent/Non-Independent Directors is as follows; Independent Vs. Non- Independent Directors 
13. Criteria for evaluating the independence of Non-Executive Directors	Code – A. 5.3	Adopted	All of the Independent Non-Executive Directors of the Company met the criteria for independence, during the year under review as stipulated by the CBSL, SEC and ICASL guidelines, and are deemed to be independent of management and free of business or other relationships that could materially interfere with the exercising of their unfettered and independent judgement.
14. Signed Independence declaration by the Non-Executive Directors	Code – A. 5.4	Adopted	During the FY 2016/17, each Non-Executive Director submitted self-declarations affirming their status of independency in terms of the applicable rules and regulations.
15. Determination of independence of Non-Executive Directors	Code – A. 5.5	Adopted	According to the self-declarations submitted by the following Non-Executive Directors and taking into account the criteria specified, in Section 4.4 of the Corporate Governance Direction issued by CBSL, the Board deems the said Directors "Independent" as at 31 March 2017. 1. Mr S.H.J. Weerasuriya 2. Ms P.T.K. Navaratne 3. Mr S.M.S.S. Bandara 4. Mr P.C. Guhashanka
16. Appointment of an Alternate Director by an Non-Executive Director	Code – A. 5.6	Adopted	Not applicable as no Alternate Director was appointed during 2016/17.
17. Senior Independent Director (SID)	Code – A. 5.7	Adopted	The requirement to appoint a Senior Independent Director does not arise under the Code, since the roles of the Chairman and the CEO are segregated and held by two different individuals.
18. Confidential discussion with SID	Code – A. 5.8	Adopted	Refer Code – A. 5.7 above.
19. Meeting of Non- Executive Directors	Code – A. 5.9	Adopted	During the year under review, the Chairman met the Non-Executive Directors once without the presence of Executive Directors.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
20. Recording of concerns in Board minutes	Code – A. 5.10	Adopted	The concerns raised by the Board during the Board meetings were discussed and recorded by the Company Secretary in the Board Minutes. There were no issues or concerns raised that could not be unanimously resolved, requiring that such matters be recorded.
A.6. Supply of information	**Principle – A.6**	Adopted	Comprehensive information is an essential part of the decision making process. The Financial and Non-Financial information is analysed and circulated seven days prior to the Board meeting to make informed and accurate decisions.
21. Information to the Board by Management	Code – A. 6.1	Adopted	The Senior Management of the Company ensure that the Board is provided with timely, accurate, relevant and comprehensive information before the Board meeting every month, through the provision of Board papers and other updates. This enables the Board to review the material presented and prepare for discussions in a timely manner, and make inquiries for additional information from the Management as and when as necessitated.
22. Adequate time for effective Board meetings	Code – A. 6.2	Adopted	The meeting agenda and the Board papers are circulated by the Company Secretary seven days prior to Board meetings, providing the Directors with adequate time to study the papers and prepare themselves for constructive discussions at Board meetings.
A.7. Appointments to the Board ☑ G4-40	**Principle – A.7**	Adopted	The Nomination Committee was established in 2013 with the chairmanship of Mr. Saro Weerasuriya, who is also the Independent Non-Executive Chairman of the Company. The terms of reference of the committee provides a formal and transparent procedure for the appointment of new Directors to the Board.
23. Nomination Committee	Code – A. 7.1	Adopted	After a comprehensive examination and an extensive screening process, the Nomination Committee recommends potential candidates who are eligible as new appointments to the Board. Based on such recommendations final decisions on appointment/re-election are made by the Board in an objective and transparent manner. During the period under review, no new appointments were made to the Board under the recommendation of the Committee. Refer Board Committee table on Page 190 for the Nomination Committee's composition, attendance at Committee meetings and other related details. The Nomination Committee Report for the financial period 2016/17 is given on Page 283.
24. Assessment of Board Composition by the Nomination Committee	Code – A. 7.2	Adopted	The Board assessed the Board members, by using the annual self-assessment process, to determine whether the Board collectively possessed the required skills, experience and the exposure among the Directors to meet the strategic demands faced by the Company and the findings of these assessments were taken into consideration in the appointment of new Directors. The complexities associated with the LFC sector in terms of business dynamics, regulatory changes and other relevant factors that took place during the financial period, were also reviewed by the Committee. The Board determined that there was no necessity for the appointment of any new Directors during the financial period.
25. Disclosure of new Director appointments to Shareholders	Code - A. 7.3	Adopted	The shareholders will be kept informed of all new appointments to the Board, with sufficient details, via immediate notification to the Colombo Stock Exchange and subsequently through the Company's Annual Report. Prior approval for appointment of new Directors is obtained from the Central Bank of Sri Lanka in terms of the applicable regulations. There were no new Board appointments for the year 2016/17.
A.8 Re-election	**Principle – A.8**	Adopted	The Directors, who are retiring by rotation, were recommended by the Nominations Committee at the AGM for shareholder approval. One-third of the Directors for the time being are required to submit themselves for re-election by the shareholders at every AGM. The Managing Director while holding office will not be subject to retirement by rotation.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
26. Appointment of Non- Executive Directors	Code – A. 8.1	Adopted	As explained in Principle A.8 above, the following Executive Directors retire by rotation in the financial year 2016/17 and are eligible for reappointment: 1. Mr. P. M. Amarasekara 2. Mrs. A. M. Ondaatjie 3. Mr. T. J. Ondaatjie
27. Election of Directors by Shareholders	Code – A. 8.2	Adopted	As explained in Principle A.8 above.
A.9 Appraisal of Board Performance	**Principle – A.9**	Adopted	It is necessitated that the members of the Board assess their own performance periodically to ensure that Board responsibilities of the Directors are satisfactorily discharged. This need has been recognised by the Board as an essential aspect towards the effective functioning of the Board.
28. Appraisal of Board performance	Code A. 9.1	Adopted	The Board carried out a comprehensive self-assessment for the FY 2016/17, of its performance and its committees. This year, the criteria of the assessment was revised and enhanced to keep abreast with the developments of the LFC sector specifics. The assessment mainly focused on the Board's contribution towards developing and monitoring strategy, the mix of knowledge and skills between the Board and Sub-Committees, the Board's commitment towards enhancing Economic, Social and Environmental Value, ensuring robust and effective risk management, quality of the relationships with the management, employees and shareholders, and ensuring proper functioning of Board Sub-Committees. A summary report of all the assessments made was tabled at the Board meeting, which highlighted areas requiring improvements to ensure the efficiency and effectiveness of the Board.
29. Annual self-assessment of the Board and its Committees	Code – A. 9.2	Adopted	The self- assessment carried out by the Board in 2016/17 included an evaluation of the performance of the Board as a whole as well as of its sub Committees.
30. Disclosure of the method of Appraisal of Board and Board Sub-Committee performance	Code – A. 9.3	Adopted	The Chairman and the Company Secretary gave their fullest cooperation and led the process of self- assessment by the members of the Board. Views of all Directors were canvassed in respect of the performance of the Board as a whole as well as of its Committees by requiring the individual Directors to complete a comprehensive evaluation form. The full results of the Board evaluations were then analysed by the Company Secretary and the findings were presented to the Board.
A.10 Disclosure of information on Directors	**Principle – A. 10**	Adopted	The disclosure of information pertaining to all Board Directors is made available to the shareholders through the Annual Report.
31. Director Information	Code – A. 10.1	Adopted	The following information pertaining to Directors is provided in the Annual Report:

Information	Pages
Brief Profile with Qualification, Experience and Expertise	176 to 177
Composition of the Board Sub-Committees	281 to 285
Board Expertise Matrix	197
Directors' Interest in Transactions	277 & 278
Directors' Shareholdings	113
Directors' Remuneration	308
Directors' Attendance at Board Meetings	190 to 193
Directors' Attendance at Sub-Committee Meetings	190 to 193

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
A. 11 Appraisal of the Chief Executive Officer	**Principle – A.11**	Adopted	As the apex Executive of the Company, the Managing Director (MD) / CEO is responsible for the day to day operations of MI with the assistance of the Senior Management and is accountable to the Board to recommend the Company's strategy and its subsequent implementation, Company performance and to ensure that appropriate internal controls are in place to manage and assess risk and that they are fully complied with.
32. Targets for the Managing Director	Code – A. 11.1	Adopted	The Managing Director (MD) is entrusted with the management of the Company's operations with decision making authority and he is fully accountable to the Board on attaining strategic targets, giving necessary consideration to market realities and changes in strategic variables. The Board, upon approving the Strategic Plan of the Company tasks the Managing Director and Corporate Management team with the responsibility of achieving the strategic targets set. At the commencement of the financial period, the Board in consultation with the Managing Director established financial and non-financial targets that were expected to be accomplished by the MD in line with the short, medium and long term objectives of the Company.
33. Evaluation of MD's Performance	Code – A. 11.2	Adopted	MD's performance assessment by the Board is an on-going process. The performance of the MD is evaluated by the Board at the end of each financial year by comparing the performance of the Company with the financial and non-financial targets set at the beginning of the financial year.
B. Directors' Remuneration **B.1 Remuneration Procedure**	**Principle – B.1**	Adopted	The Board recognises that the existence of a formal and transparent remuneration procedure supports alignment of the Directors' interests with those of shareholders; therefore no Director is involved in deciding his or her own remuneration package.
34. Remuneration Committee	Code – B. 1.1	Adopted	The Board has established a Remuneration Committee, which is authorised to evaluate and recommend Executive Directors' remuneration as per the Board approved Remuneration Committee terms of reference. Refer the Remuneration Committee Report on Page 282
35. Remuneration Committee Composition	Code B. 1.2	Adopted	All the three (3) members of: The Remuneration Committee Directors are Non-Executive Directors and the Chairman of the Committee is appointed by the Board.
		Adopted	The Remuneration Committee comprises of the following three (3) Non-Executive Directors; » S.H.J. Weerasuriya (Chairman) » P.T.K. Navaratne » N.H.V. Perera The Report of the Remuneration Committee is given on Page 282. The details of meetings held and participation status is given on Page 190
36. Remuneration of Non-Executive Directors	Code B. 1.3	Adopted	The Board as a whole decides the remuneration of the Non-Executive Directors, including the members of the Remuneration and Nomination Committee. The Non-Executive Directors receive a fee for attending meetings of the Board and Board Committees. Fees paid to the Non-Executive Directors are neither performance related nor pensionable.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
37. Remuneration Committee's access to Managing Director and professional advice	Code B. 1.4	Adopted	The Terms of Reference of the Remuneration Committee empowers it to seek appropriate professional advice internally and from external sources as and when it is deemed necessary by the Committee. When deciding on the remuneration of other Executive Directors, the Committee obtains advice from the Managing Director as necessitated other than for that of the Managing Director.
B.2 The level and make up of Remuneration structure	**Principle – B.2**	Adopted	Senior Executive positions are filled with individuals of high calibre, extensive experience and skills, whose recruitment is approved by the Board to ensure that such high calibre professionals are attracted and retained by the Company. The Board together with the Nomination Committee is aware of the importance of having in place a structure that rewards and recognizes the performance of such individuals, since the composition of the remuneration and benefits package offered to such individuals is a critical success factor in their retention and motivation. The Company's remuneration policy has been devised in a manner that considers retention and motivational requirements. The individual's performance is assessed based on individual targets and goals which are appraised annually. Bonuses, increments and career advancement opportunities are linked to these appraisals.
38. Managing Director's Remuneration	Code – B. 2.1	Adopted	The alignment between Executive Director Remuneration and the Company's strategic goals and targets is ensured by the Remuneration Committee. To ensure fair policy on remuneration, all Executive Directors including the Managing Director are afforded with a suitable and competitive remuneration package, as the Board is aware that the remuneration of Executive and Non-Executive Directors should reflect the market expectations and is adequately sufficient to attract and retain the quality personnel needed to run the Company.
39. Comparison of Remuneration with other Institutions	Code – B. 2.2	Adopted	Taking the fiercely competitive environment into consideration, the Remuneration Committee as well as the Board is aware that reward and recognition strategies together with remuneration and benefit packages should be designed to attract, motivate and retain high-calibre people, at all levels of the organisation. Therefore, the remuneration structure of the Company is reviewed from time to time with comparison to that of peers in the industry. This mechanism ensures that remuneration packages of the Executive Directors are on par with the industry/market while ensuring alignment with the Company's strategic, short term and medium term objectives.
40. Remuneration comparison with other Group Companies	Code B. 2.3	Adopted	MI does not have subsidiary companies or a parent Company under its structure to which it could draw reference to. However, pay levels of peer Directors within the Company are considered when deciding on Executive pay and remuneration structures.
41. MD's performance related payments	Code – B. 2.4	Adopted	Refer principle B.2 and Code – B. 2.1 above.
42. Executive share Options	Code – B. 2.5	Adopted	There were no executive share option schemes offered to any Director during 2016/17 period.
43. Deciding Executive Director Remuneration	Code – B. 2.6	Adopted	The Remuneration Committee drew reference to the provisions set out in Schedule E of the Code, when deciding remuneration of Executive Directors. Please see comments given in Principle B.2 for details on Executive Director Remuneration. There were no long-term incentive schemes or share option schemes proposed for Executive Directors during this period.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
44. Early termination clauses in service contract of Directors	Code – B. 2.7	Adopted	The need to incorporate early termination compensation commitment clauses in service contracts will be looked into next financial year.
45. Early terminations of Directors	Code – B. 2.8	Adopted	No terminations were effected during FY 2016/17.
46. Level of Remuneration of Non-Executive Directors	Code B. 2.9	Adopted	The Non-Executive Directors are paid a fee for attending main Board meetings and Board Sub-Committee meetings. No share option schemes were afforded to Non-Executive Directors during FY 2016/17.
B.3 Disclosure of Remuneration	**Principle – B.3**	Adopted	The remuneration policy of the Company commensurate with performance targets, it is competitive, and it reflects the performance of the business. A disclosure on Company's remuneration policy is provided on Page 282. Details of remuneration of the Board as a whole is mentioned in Code B. 3.1 below.
47. Names of members in the Remuneration Committee and remuneration paid to Directors	Code – B. 3.1	Adopted	Details of Remuneration Committee composition with meetings held and participation status of members is provided on page 190. Details on remuneration paid to Executive and Non-Executive Directors in aggregate is disclosed in page 308, in note no. 13.1 to the financial statements.
C. Relations with shareholders **C.1 Constructive use of AGM**	**Principle – C.1**	Adopted	The Board deems it necessary that there is a constructive relationship with its shareholders, who are the Company's foremost stakeholder. Therefore through the AGM, both the Company and the shareholders have the opportunity to communicate with each other. As per the Company's policy, shareholders are encouraged to participate at AGMs and convey their views and make recommendations, in order to achieve this purpose. The notices of meetings are dispatched to the shareholders within the prescribed time periods. (Refer page 374 for further information in this regard)
48. Level of proxies at AGMs	Code – C. 1.1	Adopted	The proxy forms are made available with the Annual Report and adequate prior notice to all shareholders is provided in accordance with the Companies Act. An effective mechanism is in place through the Company Secretarial Division, to record all proxy votes lodged for each resolution, and to bring to the attention of the Chairman, the level of proxies lodged on each resolution and the number of votes for and against such a resolution.
49. Separate resolutions for each separate issue	Code – C. 1.2	Adopted	Separate resolutions are proposed by the Board on each substantial issue giving shareholders the opportunity to vote on each such issue separately. The Company passed a separate resolution for the adoption of the Annual Report of the board of Directors, the "Statement of Financial Report and the Report of the Auditors" included in the Annual Report.
50. Availability of all Board Sub-Committee Chairmen at the AGM	Code – C. 1.3	Adopted	The Chairpersons of all the Board Sub-Committees, were present to answer any questions raised by the shareholders, at the AGM.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
51. Adequate notice of the AGM	Code – C. 1.4	Adopted	The Annual Report including the Financial Statements and notice of the meeting are sent to shareholders at least 15 working days prior to the date of the AGM, by the Company Secretary complying with the Companies Act No. 07 of 2007 as amended. The Annual Report for the financial year ending 2015/16 was submitted to the CSE on 21st June 2016 and was delivered to all shareholders on the same day. The Company's AGM was held on 14th July 2016. This mechanism improves the stewardship and transparency of the Company's activities, performance, and provides the opportunity to shareholders to review progress early and present their views and seek clarifications at the AGM.
52. Voting procedures at General Meetings	Code – C. 1.5	Adopted	The Company has sent the procedure relating to voting at the Annual General Meeting, which is clearly mentioned in the Notice of Meeting to each shareholder of the Company. The Notice of Meeting for the AGM for the financial year ending 2016/17 contained the procedures governing voting and were sent to the shareholders 15 working days prior to the date of the AGM.
C.2 Communication with Shareholders	**Principle – C.2**	Adopted	A meaningful engagement with all stakeholders is recognised as a top priority of the Board, and hence the Board continues to have an effective on-going dialogue with all key stakeholders, either directly or through various corporate communication channels as given on pages 41 to 43. Therefore, building and maintaining good stakeholder relationships helps the Company manage and respond to expectations, minimize reputational risk and help build strong partnerships, all of which support the commercial sustainability of the organisation. Pages 41 to 43 provides additional disclosure on the shareholder communication process with the Company.
53. Channel to reach all shareholders of the Company	Code – C. 2.1	Adopted	Out of many channels that the Company utilises to reach its shareholders in order to disseminate timely information, the holding of the Annual General Meeting and circulation of the Annual Report remains the main channel of communication. Annual and Interim Reports which contain critical financial information and other key information are made available to shareholders via the CSE website or by registered post as per the Communication Policy of the Company.
54. Policy and methodology for Communication with shareholders	Code – C. 2.2 & C. 2.3	Adopted	The Company has in place a comprehensive policy that governs communications with its different stakeholders, including shareholders. The Board approved "Communication Policy" Document was communicated to divisional heads, who in turn adopted the required communication policies and methods and cascaded the policy throughout their divisions.
55. Disclosure of Contact person for shareholders	Code – C. 2.4	Adopted	The persons who are responsible for communications with different stakeholders of MI are clearly specified in the MI Communication Policy.
56. Process to make aware of major issues and concerns of shareholders	Code – C. 2.5	Adopted	The Company Secretary maintains records of all correspondence received from shareholders and directs same to the Board or individual Director/s as applicable. Significant issues and concerns of shareholders are referred to the Board. After receiving instructions from the Board on issues and concerns referred to their attention, the Company Secretary reverts to the respective shareholder with an appropriate response. When reverting to shareholders, the Secretary is empowered to decide on the most appropriate channel of communication based on the materiality of the matter.
57. Person to contact in relation to shareholder matters	Code – C. 2.6	Adopted	Shareholders can contact the Company Secretary for any queries they may have. In addition, the Company has established a separate open door policy which invites any shareholder to contact any Executive Director or members of the Corporate Management in seeking information and assistance.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
58. The process in responding to shareholder matters	Code – C. 2.7	Adopted	Refer comment on Principle C.2.5 above.
C.3 Major transactions	**Principle – C.3**	Adopted	The Board recognizes that timely disclosure of market sensitive information is essential in maintaining investor confidence. Hence, an established process is in place to disclose any material transactions that would alter or vary the net asset position of the Company either through the annual audited Financial Statements, interim results or through announcements made to the CSE. The Board has established a Related Party Transaction Review Committee, to focus on this critical area to capture and disclose price sensitive market information through formal channels.
59. Disclosure of material facts on major transactions	Code – C. 3.1	Adopted	During the financial year 2016/17, there were no major or material transactions entered into by the Company or committed by the Company as prescribed by the Code that required disclosure to the shareholders.
D. Accountability and Audit **D.1 Financial reporting**	**Principle – D.1**	Adopted	Determining the nature and extent of the significant risks it is willing to take, in achieving its strategic objectives, is one of the prime responsibilities of the Board. The Company's performance and position for the FY 2016/17, was presented through the Financial Statements, which expressed a true and fair view.
60. Balanced and understandable assessment of the Company	Code – D. 1.1	Adopted	The Board takes on the responsibility of presenting a true and fair view in preparing the Financial Statements of the Company which are accompanied with detailed discussions and analysis in assessing the performance of the Company which facilitate the ease of understanding, when releasing /disseminating the annual and interim results and other public reports as well as reports to the respective regulators as well as information required to be furnished by statutory bodies, the Company complied with applicable Sri Lanka Financial Reporting Standards (SLFRS / LKAS) and other regulations specified, in the Finance Business Act, Colombo Stock Exchange Listing Rules and the Companies Act No. 07 of 2007 as amended. During the financial year ended 2016/17, the interim results and annual financial statements were published on a timely basis and regulatory reports were filed by the due dates.
61. Directors' Report	Code – D. 1.2	Adopted	Annual Report of the Board of Directors on the affairs of the Company is given on pages 271 to 276 covering all areas of this section.
62. Directors' and Auditors' responsibility statement	Code – D. 1.3	Adopted	The Statement of Directors' Responsibilities is given on page 279 while Auditors responsibility is clearly stated in the Auditors Report to the Financial Statements given on page 170. Further, the responsibility of Directors is outlined in the Directors' Statement on Internal Control on page 286.
63. Management Discussions and Analysis	Code – D. 1.4	Adopted	"Management Discussion and Analysis" given on pages 53 to 170 covers all the requirements of this section by providing a comprehensive commentary of the Company's performance.
64. Directors' affirmation of going concern	Code – D. 1.5	Adopted	The Annual Report of the Board of Directors confirms that the Company is a Going Concern as contained on page 275.
65. Calling of an EGM when net assets fall below 50% of shareholders' funds	Code – D. 1.6	Adopted	The net assets were well above this requirement during the year 2016/17 and the likelihood of such an adverse situation is remote. However, if such a situation was to arise, an EGM will be called and shareholders will be duly notified as per the stipulated timelines and procedure.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
66. Adequacy and accuracy of related third party transaction disclosures	Code – D. 1.7	Adopted	The Company has a Related Party Transaction (RPT) policy in place, whereby the categories of persons who shall be considered as "related parties" have been identified. In accordance with the RPT Policy, self-declarations are obtained from each Director for the purpose of identifying related parties coming under the "related party" definition. Based on the information furnished in these declarations, an "Interest Register" is maintained under the coordination of the Company Secretary to record related party transactions as and when they occur. To further strengthen the above process, a Board Related Party Transactions Review Committee was established in 2015 on a voluntary basis. Refer Related Party Transactions Review Committee Report, given on page 285 for the detailed Committee information, and the Financial Statements notes given on pages 290 to 294 for details on related party transactions for the financial year 2016/17.
D.2 Internal Controls maintaining a sound system of internal controls	**Principle – D.2**	Adopted	The Directors of MI are responsible for the Company's system of internal control and for maintaining and reviewing its effectiveness from both a financial and an operational perspective.
67. Reviewing effectiveness of internal control system	Code – D. 2.1	Adopted	The Company adopted a set of Board approved internal control policies and procedures, to evaluate the methods and procedures for risk management, implementation of the corporate governance framework and compliance with related laws and regulations. The control system is designed to counter potential risks that could arise from dealing with financial transactions or risks that could arise from other event changes in the environment and business conditions. This internal control framework also aims to safeguard shareholders' investment and the Company's assets and to ensure the reliability of its financial record keeping and reporting. Report by the Board on Internal Controls provided on page 286 complies with the content of Annexure K of the code. The Integrated Risk Management Committee and the Audit Committee assisted the Board in reviewing all associated critical risk factors and monitored the effectiveness of risk mitigating mechanisms in place. The Integrated Risk Management Committee Report on page 281 provides further information with this regard.
68. Internal Audit function	Code – D. 2.2	Adopted	The Company has its own in-house Internal Audit Department, which conducts independent audits in areas of potential risk including all branches in keeping to the annual audit plan. Auditing of the potentially high risk areas of the business is outsourced to Ernst and Young Advisory Services (Pvt) Limited.
69. Audit Committee to review process and effectiveness of risk management and internal controls and to report to the Board	Code – D. 2.3	Adopted	The Internal Audit Department carried out regular audit reviews on the risk identification and management processes and internal control systems in place including internal controls over financial reporting. The findings were reported to the Audit Committee. The Audit Committee jointly with the IRMC undertook a detailed review of the process to assess the effectiveness of the embedded controls and risk management measures. Embedded controls in existing systems and processes were strengthened or redesigned to ensure effectiveness and procedures to identify, control and report on the major risks such as credit, market, liquidity and reputation risks were revamped where applicable. The Audit Committee's findings on internal controls and risk management functions are submitted at the meetings of the Board periodically. Refer to the Report by the Board on Internal Control over Financial Reporting, Page 286.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
70. Statement of Internal Control	Code – D. 2.4	Adopted	The Report by the Board on Internal Controls given on page 286 complies with the contents in Annexure K of the Code. Some of the salient aspects highlighted are; » External Auditors review of the content of the Board's internal control statements and issue of an opinion that the process in place is in-line with the statement. » Internal Control linkage to Financial Reporting. » Audit Committee's role in reviewing internal controls. » Mechanism to identify, evaluate and manage risks.
D.3 Audit Committee – A Committee to review financial reporting aspects, internal controls and maintaining relationships with Company Auditors	**Principle – D.3**	Adopted	The Audit Committee assisted the Board of Directors in its oversight of financial reporting, internal controls and functions relating to internal and external audits. The terms of Reference of the Audit Committee, which is periodically reviewed and revised with the concurrence of the Board of Directors, clearly defines the role and the responsibility of the Audit Committee.
71. Audit Committee composition	Code – D. 3.1	Adopted	The Audit Committee comprised of three Directors, all of whom were Non-Executive. Two Directors of the Committee were Independent Non-Executive Directors. The names of members forming the Audit Committee, their attendance level, secretary and invitees of the Committee are disclosed on pages 190 and 284
72. Reviewing objectivity, effectiveness and independence of External Auditors	Code – D. 3.2	Adopted	The External Auditor's independence, objectivity and the effectiveness is reviewed by the Audit Committee. In reappointing the external auditors, the Audit Committee takes into account the relevant professional and regulatory requirements and assesses performance against Audit engagement terms. Messrs BDO Partners were re-appointed by the Audit Committee as the External Auditors for financial year 2016/17.
73. Terms of Reference of the Audit Committee	Code – D. 3.3	Adopted	The Board Audit Committee operated within clearly defined Board approved Terms of Reference. The Committee duties and responsibilities are as set out in the said Terms of Reference and are in line with the Code and the directions issued by the Chartered Accountants of Sri Lanka and Securities and Exchange Commission of Sri Lanka. Refer Audit Committee Report on page 284.
74. Disclosures of the Audit Committee	Code – D. 3.4	Adopted	The Audit Committee of the Company comprised the following Directors, S.M.S.S. Bandara (Chairman)-Independent Non-Executive Director S.H.J. Weerasuriya-Independent Non-Executive Director N.H.V. Perera-Non-Executive Director The External Auditors for the FY 2016/17, Messrs BDO Partners, Chartered Accountants have provided a declaration of their independence to the Audit Committee. Information regarding the objectives and duties of the Audit Committee is given in page 284. The Committee report clearly specifies the determination made by the Committee in relation to External Auditors' independence.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
D.4 Code of Business Conduct & Ethics	**Principle – D.4**	Adopted	A comprehensive Board approved human resource policy document is in place defining HR policies and procedures to all staff. The HR policy document of the Company upholds best corporate practices on HR management and lays the guidelines for employees to uphold sound business conduct. The approach to ethics considers the impact of actions on a broad range of stakeholders and to the reputation of the Company.
75. Compliance to requirements on business conduct and ethics	Code – D. 4.1 ☑ G4-56	Adopted	The Company has in place a comprehensive HR policy on Business Conduct and Ethics applicable to all Directors and employees at MI. The "Human Resource Handbook", which sets out HR policies that include rules on business conduct and values, for staff to adhere, has already been circulated to all the Directors and employees. A declaration was made by the Board stating "All members of the Board of Directors and key management personnel have complied with the code of business conduct and ethics introduced in the HR Handbook", in 2016/17 Director's Report given on pages 275 to 276.
76. Affirmation by Chairman that no individual has violated business conduct and ethical requirements of the Company	Code – D. 4.2	Adopted	Refer the "Chairman's Message" on page 19 for the affirmation stating that no individual has violated business conduct and ethical requirements of the Company.
D.5 Corporate Governance disclosure	**Principle – D.5**	Adopted	The Board of Directors of the Company continues to focus on improving its effectiveness, responding appropriately to new developments taking place in the business environment and making improvements to the governance framework towards continuous improvement.
77. Disclosure on Corporate Governance	Code – D. 5.1	Adopted	The Corporate Governance Report from Pages 182 to 242 sets out the manner in, and the extent to which the Company has complied with the Code.

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
Section 2 – Shareholders: E. Institutional Investors			
E.1 Shareholder Voting	**Principle – E.1**	Adopted	The Company promotes an open communication policy with all shareholders, transparently and regularly in order to facilitate mutual understanding between the two parties. The Company encourages all shareholders to participate at the Annual General Meeting (AGM). This way, both the Board and the Senior Management are accessible to the investors.
78. Constructive dialogue between shareholders and the Company.	Code – E. 1.1	Adopted	The AGM is used as a forum for the shareholders to express their views and communicate matters that are relevant to the general membership. From the Company's perspective, the AGM provides a forum for the Company to inform the shareholders how it has performed during the year. Shareholder views and other matters are taken up at Board and Sub-Committee meetings depending on the materiality and urgency of the matter at hand. The opinions and views of shareholders on material matters were communicated to the Board and Senior Management by the Company Secretary.
E.2 Evaluation of Governance Disclosure	**Principle – E.2**	Adopted	Matters relating to Corporate Governance along with the adequate disclosures are communicated to all shareholders via the Annual Report and at the AGM as mentioned above.
F. Other Investors F.1 Individual shareholders	**Principle – F.1**	Adopted	The Company places a high degree of importance on maintaining good relationships and communications with individual shareholders and ensures that they are kept informed of significant developments of the Company as well as the LFC sector. Individual shareholders are encouraged to carry out their own analysis or seek independent advice on investing, holding or divesting decisions. Quarterly published accounts in the CSE site will assist the retail investors to make judgments on the performance of the Company.
F.2 Shareholder voting	**Principle – F.2**	Adopted	Institutional shareholders, being the main component of investors, are encouraged to participate at the Annual General Meeting and cast their votes. In order to achieve this purpose, the notices of the meeting are dispatched to all shareholders within the prescribed time periods. The AGM provides the opportunity for the Board to meet investors and for the Chairman to explain the Company's progress and receive questions from the shareholders.

Corporate Governance Report

Corporate Governance Principles	Reference to SEC & ICASL Code	Adoption Status	Status of Adoption (2016/17 Update)
G.Sustainability Reporting	**Principle – G.1**	Adopted	The Company recognises that a sustainability report presents the organisation's values and governance model, and demonstrates the link between its strategy and efforts at maintaining a sustainable enterprise and also its commitment to a sustainable global economy. Being a responsible corporate citizen, we believe in meeting most of the responsibilities towards key stakeholders namely; shareholders, customers, employees, suppliers and the community in the optimal way through our business activities. We have embraced suitable sustainability strategies to enhance the Company's impact on the economy, society and the environment in keeping to our sustainability vision, goals and ideologies as explained on pages 75,95,117,128,135 and 145. The Annual Report for the financial year 2016/17 has been prepared in the form of an integrated report covering all sustainability reporting parameters as required by the Global Reporting Initiative (GRI) guidelines and wider economic impact on pages 74 to 169 which cover the requirements of this section.
79. Economic Sustainability	Code – G. 1.1	Adopted	Refer Financial Capital, Pages 74 to 93
80. Environmental Sustainability	Code – G. 1.2	Adopted	Refer Natural Capital, Pages 134 to 143
81. Labour practices	Code – G. 1.3	Adopted	Refer Human Capital, Pages 116 to 127
82. Society governance disclosures	Code – G. 1.4	Adopted	Refer Social Capital, Pages 144 to 154
83. Product responsibility disclosures	Code – G. 1.5	Adopted	Refer Relationship Capital, Pages 94 to 115
84. Stakeholder identification, engagement and effective communication	Code – G. 1.6	Adopted	Refer Stakeholder Engagement, Pages 41 to 43
85. Formalised Sustainability Reporting Process	Code – G. 1.7	Adopted	Refer About this Report, Pages 5 to 8

Mercantile Investments and Finance PLC's Compliance with Finance Companies (Corporate Governance) Direction No. 3 of 2008 as amended by Directions No. 4 of 2008 and No. 6 of 2013 issued by The Central Bank of Sri Lanka ("Corporate Governance Directions")

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Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
2. The Responsibilities of the Board of Directors a. Approving, overseeing and communicating the finance company's strategic objectives and corporate values.	Complied	The strategic objectives of the Company were set at the Board level, and it revolved around gaining a higher market share and delivering above average market returns to enhance investor value and meet stakeholder expectations. The second consecutive Board approved strategic plan developed for the medium term specified strategic objectives, corporate values and the risk management policy, and Risk Appetite of the Board in keeping with overarching philosophy of prudence, the vision and mission statements of MI. In setting the strategic objectives of the Company, the Board of Directors considered the expectations of all key stakeholders in addition to those of the investors. The strategic objectives set were communicated to all divisional heads through a presentation of the strategic plan, in order that each division was given the opportunity to plan their individual operational targets to achieve the corporate goals and to communicate the required resource requirements to the corporate management. The Company demonstrated a top down and bottom up approach to communication, where insights towards setting the strategic objectives were obtained from across the organization and the goals and strategic actions were communicated to the staff through the organizational hierarchy. MI Board provides oversight over key matters including strategy by delegating key areas to its Board Sub-Committees and corporate management. They are expected to provide continuous feedback on all concerns and recommendations to the Board to take ultimate decisions.
b. Approving the overall business strategy of the finance company, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least the immediate three years to follow.	Complied	The strategic plan covering a three year period up to 2017/18 was approved by the Board on 30th June 2015. The strategy formulation process revolved around formulating separate strategies for core businesses and support functions of the Company for the attainment of the overall corporate objectives with measurable goals and time lines being stipulated over the three year duration of the plan. The Company's risk policy was developed, formulated and approved, by the board in keeping to MI's successful strategic framework that is well aligned with the Company's overall risk management strategy. The risk management policy of the Company, addresses how risks are identified, and it defines the risks of the Company and the procedures and processes to manage and/or mitigate the risks and bring them within tolerance of acceptable levels to safeguard MI's six forms of capital and to prudently manage MI's operations. It clearly defines the Risk Appetite of the Company in setting limits for the key risks identified.
c. Identifying risks and ensuring implementation of appropriate systems to manage the risks prudently.	Complied	The Board places significant importance in shaping the Company's risk management policy and procedures to effectively manage risks arising from executing strategy and related operational activities. The Integrated Risk Management Committee, on behalf of the Board, identifies risks and provides oversight to ensure the implementation of appropriate systems and processes to manage risks prudently and reports to the Board on a quarterly basis. The committee obtains information directly from both the Manager Risk and Compliance and the Corporate Management.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
d. Approving a policy of communication with all stakeholders, including depositors, creditors, shareholders and borrowers.	Complied	The Board approved communication policy issued in 2011 which demonstrates the manner in which the Company communicates with its key stakeholders. The policy specifies the communication approach and methods to be adopted when dealing with various external parties. Numerous effective communication methods and channels are specified in dealing with the Company's list of stakeholders.
e. Reviewing the adequacy and the integrity of the finance company's Internal Control System. Reviewing the adequacy and the integrity of the finance company's Management Information Systems.	Complied Complied	The Board has established a comprehensive system of internal controls to manage risks associated with the business. The Board has delegated its authority to The Audit Committee, who on behalf of the Board monitors the effectiveness of the internal control systems on a continuous basis and reports to the Board on its findings. The Board approved procedures are well embedded into the work ethic and culture of the organization and tested periodically for effectiveness and compliance through the periodic external and internal audits carried out. The Audit findings are discussed in detail with the Board Audit Committee with the Management being given the opportunity to respond to the audit findings. There is a continuous review of the Company's management information systems, with specific focus on the accuracy, timeliness and security of the systems. During the FY 2016/17 Ernst & Young conducted a comprehensive system audit on the SLIPs process. An audit of the deposit system is currently in progress.
f. Identifying and designating key management personnel, who are in a position to: i. Significantly influence policy; ii Direct activities; and iii Exercise control over business activities, operations and risk management.	Complied	The Directors, Senior Management, Compliance Officer, Head of Internal Audit and Company Secretary have been identified and designated as the Key Management Personnel of the Company. They possess the required qualifications and experience to hold such positions and have been given clear job roles to exercise effective control over their respective functions.
g. Defining the areas of authority and key responsibilities for the Board and for the key management personnel.	Complied	A document titled, "The Board's Responsibility" has been prepared illustrating each Board members role, specifying job descriptions for the Managing Director, Chairman, Executive Directors and the Non-Executive Directors. Executive Directors and the Corporate Management are expected to carry out their duties and their responsibilities, based on the delegated authority of the Board and in line with their formal job description designed for each of the top managerial positions and in keeping with limits of authority prescribed for the carrying out of business operations.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
h. Ensuring that there is appropriate oversight of the affairs of the finance company by key management personnel, that is consistent with the finance company's policy.	Complied	At monthly Board meetings, the Directors review the Company's performance and monitor the key areas of business on an on-going basis. Feedback is provided on any material matters to the Board by various Board Sub-Committees appointed by the Board to provide oversight and monitoring of strategic issues and functional areas of business. The Board also through the delegation of authority to the Managing Director has given him accountability in implementing the decisions of the Board and managing the performance and affairs of the Company in line with his delegated limits of authority. The Managing Director, in turn, delegates the responsibility of managing the key operational functions to senior heads at corporate management level in overseeing performance and managing operations effectively as per the approved limits of authority. The Directors either directly or through the Board Sub-Committees, initiate periodic meetings with the Corporate Management. Department specific meetings are also held and include Credit, Marketing and Recoveries meetings that enable the Corporate Management to keep a close watch on the operations, on an on-going basis.
i. Periodically assessing the effectiveness of its governance practices, including: i. The selection, nomination and election of Directors and appointment of key management personnel; ii. The management of conflicts of interests; and iii. The determination of weaknesses and implementation of changes where necessary.	Complied	The strong corporate governance framework established by the Company is periodically assessed by the Board as follows; The Board carries out independent reviews on a continuous basis to assess the effectiveness of the overall governance framework and it's adherence to applicable regulations. To bridge gaps identified, the Board takes numerous measures which include the establishing of best practice guidelines to improve the existing framework as necessary. A self-evaluation of the Board was carried out in the last quarter of the financial year 2016/17, and feedback of the Directors therein was discussed at the subsequent Board meeting. The Code of Best Practice on Corporate Governance issued by the ICASL and the SEC provides for the general procedure applicable to selection and appointment of Directors of the Company. Presently, all new appointments and re-elections to the Board are recommended by the Nominations Committee. Any new appointments will be approved by the Board itself, but all re-elections will be done by the shareholders at the AGM. The Key Management Personnel, have been duly selected, recruited and retained by the Managing Director on the approval of the Board. The Management of conflicts of interests is addressed in the terms of reference of the Related Party Transaction Review Committee of the Company. A self-declarations on potential conflicts of interests are obtained from the Directors at the time of their appointment to the Board and subsequently as and when it is required.
j. Ensuring that the finance company has an appropriate succession plan for key management personnel.	Complied	A Board approved succession plan is in place for identified key management personnel of various divisions, laying the career paths for such individuals under their respective functional areas. The succession plan was approved on 30th June 2015.

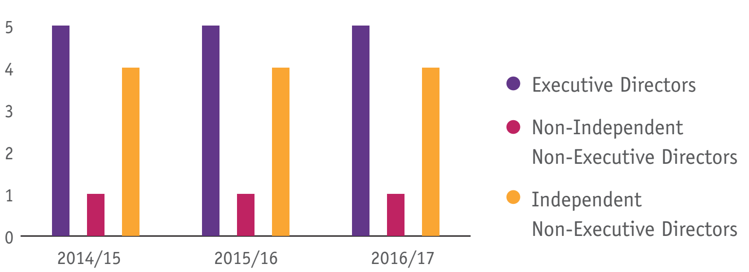
Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
k. Meeting regularly with key management personnel to review policies, establish lines of communication and monitor progress towards the corporate objectives.	Complied	Directors communicate with each other on an on-going basis apart from interacting at Board meetings. Executive Directors meet with each other and line managers frequently on routine matters. Executive Directors meet with the Corporate Management on a frequent basis, at least weekly, to assess the performance and to decide on key matters. Management Committee meetings are held comprising of the Executive Directors, Corporate Management and other Key Officers to assess the performance in each business area, in comparing actual performance with plan and benchmarking performance against the industry, and to discuss, evaluate and monitor assets and liability management actions and risk implications closely.
l. Understanding the regulatory environment.	Complied	The Board is updated with new developments and changes in the regulatory environment at Board meetings by fellow Directors and by the members of the Corporate Management via circulars, reports and presentations. As part of the Company's training and development program, Directors, Corporate Management and other key officers undergo continuous training on key technical aspects and other requirements including regulatory matters. The Manager – Risk and Compliance, as the Compliance Officer (CO) through the IRMC, follows up on the Company's adherence to regulations related to money laundering and also updates the Board on a monthly basis through the Finance Director on the compliance status of the Company in relation to CBSL directions, rules and other requirements. The advice of the Legal Division is sought by divisions as and when required and also when new regulations are imposed or when changes to existing regulations occur. Divisions maintain close coordination and rapport with the respective regulatory bodies in seeking clarification and ensuring due compliance.
m. Exercising due diligence in the hiring and oversight of External Auditors.	Complied	The hiring and oversight of External Auditors is handled by the Audit Committee on behalf of the Board. Messrs BDO Partners were re-appointed by the Audit Committee as the External Auditor of the Company for the financial year 2016/17, in accordance with CBSL regulations on selecting External Auditors for the sector that are approved by the regulator. The Committee evaluates the independence and quality of work carried out by External Auditors annually by reviewing the quality of the audit work carried out. The deliverables such as the Management letter and other opinions and reports issued by the external auditors are also reviewed in this context.
2.1 Appointment of the Chairman and the Chief Executive Officer and defining and approving their functions and responsibilities.	Complied	The functions and responsibilities of the Non – Executive Chairman and the Chief Executive Officer have been separately defined and approved by the Board. The Chief Executive Officer's role is performed by the Managing Director who leads the Executive Management team of the Company. The Chairman provides leadership to the Board to ensure the Board discharges its responsibilities effectively. The Managing Director, on the other hand, being an Executive Director oversees the effective running of the day- to- day operations of the Company.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
2.2 Availability of a procedure determined by the board to enable directors, to seek independent professional advice at the Company's expense.	Complied ☑ G4-57	In discharging their duties, any Board Director has the right to seek independent professional advice at the expense of the Company whenever needed. A formal procedure on seeking independent professional advice was approved by the Board and has been in effect since 2013. All Directors are informed of this formal procedure and can seek independent professional advice when faced with complex situations. Approval limits on related fee payments have been specified so that Directors could seek advice without delay.
2.3 Avoidance of conflicts of interest.	Complied	The Board identified the importance of avoiding matters of conflict of interest, between obligations to the Company and the personal interests of the Directors of the Board. The Board took steps to ensure that when such situations arise, Directors disclose such instances to the Board. In such instances, a Director is expected to refrain from voting or presenting their views on such matters. In keeping to best practices on the identification of related party transactions, a separate "Related Party Transaction Review Committee (RPTC)" was set up in 2015 to monitor related party transactions and report any concerns to the Board. The related parties would be disclosed by Directors at any time such a conflict arises. These related parties will then be known by the RPTC who will be informed by the finance department of such related party affiliations. A quarterly report in this regard is submitted by Manager Risk and Compliance to the RPTC, in order to review if objectivity was maintained in conducting such transactions.
2.4 A formal schedule of matters specifically reserved for the Board, to ensure that the direction and control of the Finance Company is firmly under its authority.	Complied ☑ G4-41	A formal process has been developed by the Board in order to effectively discharge Board functions. A formal schedule of matters has been approved, to ensure the direction and control of the Company is firmly under the Board's control and authority. The Board secretary circulates the agenda together with relevant supporting information to the Board members seven days prior to the Board meeting. The agenda and documents circulated under the supervision of the Chairman, ensures critical matters and general performance updates are taken up in keeping with the Board's expectations.
2.5 Disclosure of insolvency to the Director of the Department of Supervision of Non-Bank Financial Institutions.	Complied	The Company is a going concern as declared in the "Annual Report of the Board of Directors" on page 275. The Company fulfilled its obligations to all its depositors and creditors, thus there was no necessity to inform the regulator in this regard. The Company paid interest and made the requisite capital re payments as falling due to its depositors and also to the lenders of capital. The liquidity position of the Company is reported to the Director of the Department of Supervision of Non-Bank Financial Institutions on a weekly basis.
2.6 Inclusion of an Annual Corporate Governance Report on compliance with the corporate governance directions in the Annual Report.	Complied	The Corporate Governance Report given from Pages 182 to 242 provides a comprehensive disclosure of the Company's compliance status, in compliance with the direction issued by CBSL for the financial year 2016/17.
2.7 The Board shall adopt a scheme of self-assessment to be undertaken by each Director annually, and maintain records of such assessments.	Complied	The Board implemented its self-assessment mechanism, which required each Director to evaluate their performance as well as the Boards' performance collectively for the financial period 2016/17. The criteria was enhanced to include a more detailed assessment, making the self-assessment more comprehensive. The summary of findings together with areas for further improvements was tabled for the deliberation of the Board.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
3. Meetings of the Board	Complied	Twelve (12) Board Meetings were held for the financial period 2016/17.
3.1 The Board shall meet at least twelve times a financial year at approximately monthly intervals. Obtaining the Board's consent through the circulation of written or electronic resolutions /papers shall be avoided as far as possible.		Refer section A.1.1 of the SEC and ICASL code given on page 198 for full disclosure in this regard. Board papers seeking approval of the Board are taken up at Board meetings, and approved after necessary deliberation. Urgent matters needing the Directors review and approval between monthly Board meetings are obtained via circulation by the Company Secretary.
3.2 The Board shall ensure that arrangements are in place to enable all Directors to include matters and proposals in the agenda for regular Board meetings where such matters and proposals relate to the promotion of business and the management of risks of the Finance Company.	Complied	The agenda prepared by the Company Secretary under the guidance of the Chairman incorporates all proposals submitted by Directors. All Directors are provided an equal opportunity to submit proposals with regard to all key areas of business they head and to table proposals pertaining to new business development and risk management.
3.3 Notice of at least 7 days shall be given of a regular Board meeting to provide all Directors an opportunity to attend. For all other Board meetings, a reasonable notice shall be given.	Complied	The Board secretary informs Directors at least 7 days in advance of impending Board meetings and circulates the necessary Board "Information Booklet" and other additional information as necessary. This allows Directors adequate time, to review the circulated Board papers and take up concerns and raise other matters of importance at Board meetings. In addition to regular Board meetings, the Company Secretary ensures that reasonable notice is given, for any other meetings that need to be held by the Board.
3.4 A Director, who has not attended at least two-thirds of the meetings in the period of 12 months immediately preceding or has not attended the immediately preceding three consecutive meetings held, shall cease to be a Director. Participation at the Directors' meetings through an alternate Director shall, however, be acceptable as attendance.	Complied	All Directors have participated over the minimum participation requirement of at least attending two-thirds of the meetings held for the financial year 2016/17. No Directors have been absent from three consecutive Board meetings during financial year 2016/17. There were no instances where an alternate Director was required to be nominated during this financial year. Attendance status of each Director at Board meetings is given on page 190.
3.5 The Board shall appoint a Company Secretary whose primary responsibilities shall be to handle the secretarial services to the Board and shareholder meetings and to carry out other functions specified in the statutes and other regulations.	Complied	Company Secretary's responsibilities and services extended to the Board are given on page 202 of section A.1.4 of the SEC and ICASL Code.
3.6 If the Chairman has delegated to the Company Secretary the function of preparing the agenda for a Board meeting, the Company Secretary shall be responsible for carrying out such function.	Complied	The responsibility for the preparation of the agenda for Board meetings has been delegated to the Company Secretary under the supervision of the Chairman. She takes a coordinating role to circulate the agenda, dealing with Directors and Corporate Management to incorporate key matters to be taken up in the agenda. Prior to circulation, she obtains the Chairman's approval for the notice of meeting and the agenda.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
3.7 All Directors shall have access to advice and services of the Company Secretary with a view to ensuring that Board procedures and all applicable laws, directions, rules and regulations are followed.	Complied	The Company Secretary attended all Board meetings during the financial year 2016/17 and is readily accessible to all Directors should they require her advice and services. Mrs S. Pethiyagoda has over 20 years of experience in the Company Secretarial position and keeps herself updated on all current regulations applicable to Board procedures, corporate governance requirements and other requirements related to the Company Secretarial responsibilities.
3.8 The Company Secretary shall maintain the minutes of Board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any Director.	Complied	Minutes of all Board meetings held during the financial year 2016/17 was duly perfected and maintained in safe custody by the Company Secretary. The Board of Directors have access to the minutes and can inspect Board minutes at any point in time. The approval of the Chairman is obtained for the minutes prior to its circulation to Directors by the Company Secretary.
3.9 Minutes of Board meetings shall be recorded in sufficient detail.	Complied	Minutes of all Board meetings are recorded in a timely manner, in sufficient detail and retained by the Company Secretary under the supervision of the Chairman.
4. Composition of the Board		
4.1 Subject to the transitional provisions contained herein, the number of Directors on the Board shall not be less than 5 and not more than 13.	Complied ☑ G4-38	The Board comprised of ten Directors in keeping to the provisions of this section and did not fall below 5 or exceed 10 Directors due to resignations or appointments during the year. The Board composition remained unchanged with the composition that prevailed over the previous financial year. Composition of MI Board Last 3 years 

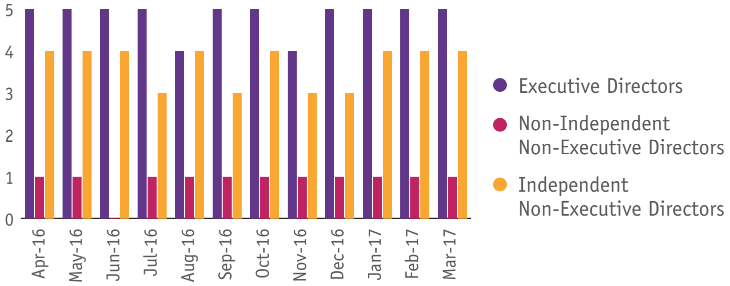
Corporate Governance Report

<table>
<tr><th>Direction Requirement
(With Section Number of the Direction)</th><th>Compliance Status</th><th>Extent of Adoption</th></tr>
<tr><td>4.2 Subject to the transitional provisions contained herein and subject to paragraph 5. (1) of this direction, the total period of service of a Director other than a Director who holds the position of Chief Executive Officer or Executive Director shall not exceed nine years.</td><td>Complied</td><td>In keeping with this section, all Non-Executive Directors' period of service did not exceed nine years as given below:
<table>
<tr><th>Name of Director</th><th>Directorship Status</th><th>Number of years in position as at 31 March 2017</th></tr>
<tr><td>Mr S.H.J.Weerasuriya</td><td>Chairman (Independent Non- Executive Director)</td><td>5 years completed</td></tr>
<tr><td>Ms P.T.K. Navaratne</td><td>Independent Non–Executive Director</td><td>5 years completed</td></tr>
<tr><td>Mr N.H.V. Perera</td><td>Non–Executive Director</td><td>5 years completed</td></tr>
<tr><td>Mr S.M.S.S. Bandara</td><td>Independent Non–Executive Director</td><td>5 years completed</td></tr>
<tr><td>Mr P.C. Guhashanka</td><td>Independent Non–Executive Director</td><td>3 years and 9 months completed</td></tr>
</table></td></tr>
<tr><td>4.3 Subject to the transitional provisions contained herein, an employee of a Finance Company may be appointed, elected or nominated as a Director of the finance company (hereinafter referred to as an “Executive Director”) provided that the number of Executive Directors shall not exceed one-half of the number of Directors of the Board. In such an event, one of the Executive Directors shall be the Chief Executive Officer of the Company.</td><td>Complied</td><td>An equal 50% representation was maintained between Executive Directors (Five Directors) and Non-Executive Directors (Five Directors) and is within the provisions of this section.

Since the Board is equally balanced between the Executives and Non-Executives, the Managing Director carries out the duties of the Chief Executive Officer at MI.</td></tr>
<tr><td>4.4 With effect from three years from the date of this Direction, the number of independent Non-Executive Directors of the Board shall be at least one fourth of the total numbers of Directors.</td><td>Complied</td><td>The Board consists of four Independent Non-Executive Directors as against a total of ten Directors (40%) and hence is within the requirement to have one fourth (25%) of the total number of Directors as Independent Non-Executive Directors.

Self-declarations were obtained from all Non-Executive Independent Directors confirming their suitability to be designated as “Independent” in terms of the criteria in this rule.

(Refer page 204 of section A.5.5. of the SEC and ICASL Code for information pertaining to Independent Non-Executive Directors.)</td></tr>
<tr><td>4.5 In the event an Alternate Director is appointed to represent an Independent Non-Executive Director, the person so appointed shall also meet the criteria that apply to the Independent Non-Executive Director.</td><td>N/A</td><td>Not applicable since there were no Alternate Director appointments necessitated during this period.</td></tr>
</table>

Direction Requirement (With Section Number of the Direction)	**Compliance Status**	**Extent of Adoption**
4.6 Non-Executive Directors shall have necessary skills and experience to bring an objective judgement to bear on issues of strategy, performance and resources.	Complied	All Non-Executive Directors have been selected to the Board based on their qualifications and experience in their respective fields. Pages 176 to 177 provides a brief on the profile of Non-Executive Directors outlining their qualifications and experience and positions they hold in other institutions. They hold senior positions in various organisations and attend Board meetings, Sub-Committee meetings and other special meetings of the Company, as and when necessary.
4.7 With effect from three years from the date of this Direction, a meeting of the Board shall not be duly constituted, although the number of Directors required to constitute the quorum at such meeting is present, unless at least one half of the number of Directors that constitute the quorum at such meeting are Non-Executive Directors.	Complied	In complying with this section, in all Board meetings convened during financial year 2016/17, the number of Non-Executive Directors present was more than one half of the number that constituted the quorum. Monthly Quorum Status of the Board Meetings 
4.8 The Independent Non-Executive Directors shall be expressly identified as such in all corporate communications that disclose the names of Directors of the Finance Company. The Finance Company shall disclose the composition of the Board, by category of Directors, including the names of the Chairman, Executive Directors, Non-Executive Directors and Independent Non-Executive Directors in the Annual Corporate Governance Report which shall be an integral part of its Annual Report.	Complied	The Annual Report distinguishes between each category of Directors, and goes on to disclose the names of each Independent Non-Executive Director in the Corporate Governance Report, in the section outlining the profiles of the Directors on pages 176 to 177. The following disclosures cover requirements of this section: » Composition of the Board is given on page 223. » Category of Directors is given on pages 203 to 204. All communications with the CSE, publications and corporate communications that disclose the names of Directors expressly identify the Executive Directors in compliance with this section. Further, the Corporate Governance Report that is contained in this report discloses the details of Directors, the composition of the Board, by category of Directors, including the names of the Chairman, Executive Directors, Non-Executive Directors and Independent Non-Executive Directors as required by this section.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
4.9 There shall be a formal, considered and transparent procedure for the appointment of new Directors to the Board. There shall also be procedures in place for the orderly succession of appointments to the Board.	Complied	The Code of Best Practice on Corporate Governance issued by the ICASL and the SEC provides for the general procedure applicable to selection and appointment of Directors of the Company. All new appointments and re-elections to the Board require the approval of the Nominations Committee. Upon the nominees being found to be "fit and proper" for appointment as Directors of the Company, approval of the Director of Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka is obtained for the same. Refer page 190 of section A.7 of the SEC and ICASL Code for details on the Nominations Committee composition, duties, related matters and the procedure followed in making appointments to the Board. The Board Nomination Committee Report is given on page 283.
4.10 All Directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment.	N/A	No Directors were appointed to fill casual vacancies during the financial year 2016/17.
4.11 If a Director resigns or is removed from office, the Board shall announce to the shareholders and notify the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka, regarding the resignation of the Director or removal and the reasons for such resignation or removal, including but not limited to information relating to the relevant Director's disagreement with the Board, if any.	Complied	Resignations of Directors are duly informed to the Department of Supervision of Non- Bank Financial Institutions and to the Colombo Stock Exchange by the Company Secretary in complying with this section and related provisions as per the Colombo Stock Exchange rules. No resignations of Directors took place during the financial year 2016/17 that warranted reporting to the CBSL.
5. Criteria to assess the fitness and propriety of Directors 5.1 Subject to the transitional provisions contained herein, a person over the age of 70 years shall not serve as a Director of a Finance Company.	Complied	No Board member is over the age of 70 years as at 31 March 2017. Page 187 provides the age profile of the Board of Directors.
5.2 A Director of a finance company shall not hold office as a Director or any other equivalent position in more than 20 companies/societies/bodies corporate, including associate companies and subsidiaries of the finance company.	Complied	As given in the matrix on Page 189 detailing Directorships held by each Director on the Board of Mercantile Investments in other companies as at 31 March 2017, no Director of the Board holds office in over 20 companies contravening the provisions of this section.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
6. Delegation of Functions		
6.1 The Board shall not delegate any matters to a Board committee, Chief Executive Officer, Executive Directors or key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the Board as a whole to discharge its functions.	Complied	The Board has delegated some of its duties to the Board Sub-Committees and to the Corporate Management, but keep close oversight over their direct reports to ensure the Board's ability to discharge its duties is not impaired at any point in time. The Board evaluated the delegated authority limits, assessing particularly the credit authority limits and other limits applicable to the Board Sub-Committees this year. The Board has delegated Directors and specified authorised signatories to approve payments and sign key binding documents limiting delegation of certain key functions.
6.2 The Board shall review the delegation processes in place on a periodic basis to ensure that they remain relevant to the needs of the Finance Company.	Complied	The Board reviewed the delegated powers vested with Directors, Corporate Management and other employees to ensure relevance to the needs of the Company. Refer comments given on 6.1 above.
7. The Chairman and the Chief Executive Officer		
7.1 The roles of Chairman and Chief Executive Officer shall be separated and shall not be performed by one and the same person after 3 years commencing from 1st January 2009.	Complied	In keeping to this section, an Independent Non-Executive Director was appointed by the Board to act as the Chairman of the Company, and there is a separate Managing Director (MD) in an Executive Director capacity. Thus, the two roles are segregated. Refer pages 202 to 203 of section A.2 and A.3 of the SEC and ICASL Code for further details.
7.2 The Chairman shall be a Non-Executive Director. In the case where the Chairman is not an Independent Non-Executive Director, the Board shall designate an Independent Non-Executive Director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the Finance Company's Annual Report.	Complied	Mr. Saro Weerasuriya, being an Independent Non-Executive Director was appointed as the Chairman to the Board in January 2011 and continued to operate in this capacity during period under review.
7.3 The Board shall disclose in its Corporate Governance Report, which shall be an integral part of its Annual Report, the name of the Chairman and the Chief Executive Officer and the nature of any relationship [including financial, business, family or other material/relevant relationship(s)], if any, between the Chairman and the Chief Executive Officer and the relationships among members of the Board.	Complied	No material relationship including financial, business or family exists between the Chairman Mr. Saro Weerasuriya and the Managing Director / Chief Executive Officer Mr. Gerard G. Ondaatjie. A declaration to this effect was obtained from the Chairman and Directors during the financial year. However, Executive Directors, Mr. Gerard G. Ondaatjie, Ms. Angeline M. Ondaatjie and Mr. Travice J. Ondaatjie are members of the same family.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
7.4 The Chairman shall: a. Provide leadership to the Board; b. Ensure that the Board works effectively and discharges its responsibilities; and c. Ensure that all key issues are discussed by the Board in a timely manner.	Complied	The Chairman of the Company provided leadership, in working closely with other Directors of the Board in all substantial matters to effectively discharge the responsibilities of the Board. The Chairman in conducting Board related affairs obtained the fullest cooperation of other fellow Directors. In like manner he sought advice from the Company Secretary on Board procedures when deemed necessary. At monthly meetings, the Chairman ensured attention was given to all matters of strategic importance to the Company. Refer pages 202 to 203 of section A.2 and A.3 of the SEC and ICASL code for further details on the Chairman's role.
7.5 The Chairman shall be primarily responsible for the preparation of the agenda for each Board meeting. The Chairman may delegate the function of preparing the agenda to the Company Secretary.	Complied	The Company Secretary prepared the formal agenda for Board meetings under the supervision of the Chairman. The agenda covered key matters to be discussed and included information on the performance of the Company for the period under review in providing the Directors with the necessary information to support informed decision making at the meetings of the Board. Under the supervision of the Chairman, all Directors are informed well in advance on key matters to be discussed at Board meetings.
7.6 The Chairman shall ensure that all Directors are informed adequately and in a timely manner of the issues arising at each Board meeting.	Complied	The agenda with notice of meeting is duly circulated to the Directors as per the stipulated timelines as given in section 3.3 in this code, giving sufficient time to the Directors to prepare themselves on the issues to be taken up.
7.7 The Chairman shall encourage each Director to make a full and active contribution to the Board's affairs and take the lead to ensure that the Board acts in the best interests of the Finance Company.	Complied	The Chairman leads from the front, in encouraging active participation of all Directors, in governing the affairs of the Company and acting in the best interest of the Company.
7.8 The Chairman shall facilitate the effective contribution of Non-Executive Directors in particular and ensure constructive relationships between Executive And Non-Executive Directors.	Complied	All Non- Executive Directors including the Chairman effectively contributed to the working of the Board, through their immense experience and knowledge gained on the finance industry and experience gained from their professional fields. All Directors were able to attend a majority of the Board meetings and contributed to matters brought up at meetings, individually as well as collectively. They were able to raise concerns, recommend suitable solutions and deliberate with each other to make effective decisions. This process is further strengthened through the self-evaluations of the Board where views of all Directors are canvassed in respect of the overall Board and its effectiveness.
7.9 Subject to the transitional provisions contained herein, the Chairman, shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever.	Complied	The Chairman, being an Independent Non-Executive Director does not directly supervise the key management personnel or handle executive duties. The duties of the Chairman have been defined and approved by the Board and do not include executive duties whatsoever.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
7.10 The Chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of shareholders are communicated to the Board.	Complied	The views of shareholders are primarily obtained at the AGM where they have the opportunity of expressing their views, voice their concerns and making recommendations for the betterment of the Company. Shareholders are also able to meet the members of the Board on a one-to-one basis, on obtaining a formal appointment. Matters raised by shareholders at the AGM are taken up subsequently and responded to in writing by the Company Secretary under the supervision of the Chairman of the Board, depending on its relevance and materiality.
7.11 The Chief Executive Officer shall function as the apex executive-in-charge of the day-to-day-management of the Finance Company's operations and business.	Complied	The Managing Director/Chief Executive Officer, Mr Gerard G. Ondaatjie, functions as the apex executive-in-charge of the day-to-day management of the Company's business operations. He works closely with other Executive Directors and the Corporate Management team to ensure the smooth running of day-to-day operations. His role and responsibilities as the Managing Director/Chief Executive Officer have been defined and approved by the Board.
8. Board appointed Committees		
8.1 Every finance company shall have at least the two Board committees set out in paragraphs 8.2 and 8.3 hereof. Each committee shall report directly to the Board. Each committee shall appoint a secretary to arrange its meetings, maintain minutes, records and carry out such other secretarial functions under the supervision of the Chairman of the committee. The Board shall present a report on the performance, duties and functions of each committee, at the Annual General Meeting of the Company.	Complied	Six (6) Board Sub-Committees have been established by the Company's Board for the provision of oversight and monitoring of the Company's affairs. The Board appointed Sub-Committees, compositions, duties and performance during the year is given on Pages 190 to 192 in the Board Committee Matrix.
8.2 Audit Committee The following shall apply in relation to the Audit Committee: 8.2(a) The Chairman of the committee shall be an Non-Executive Director who possesses qualifications and experience in accountancy and/or audit.	Complied	The Chairman of the Audit Committee, Mr. S. M. S. S. Bandara, an Independent Non-Executive Director serves as the Chairman to the Audit Committee. He is a Fellow Member of the Institute of Chartered Accountants of Sri Lanka, and also a council Member of the Governing Council of the Institute of Chartered Accountants of Sri Lanka. While possessing two accounting qualifications, he has a wealth of experience in the field of Audit, and financial reporting being a partner of B. R. De Silva, Chartered Accountants. Therefore, he is able to effectively oversee the Committee's functions.
8.2(b) The Board members appointed to the committee shall be Non-Executive Directors.	Complied	All three members of the Audit Committee are Non- Executive Directors, two of whom are Independent, and operate independently to ensure impartiality of the Committee. The Committee composition remained unchanged throughout the period. Refer page 213 of section D.3 of the SEC and ICASL code for details.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
8.2(c) The committee shall make recommendations on matters in connection with: i. The appointment of the External Auditor for audit services to be provided in compliance with the relevant statutes; ii. The implementation of the Central Bank guidelines issued to Auditors from time to time; iii. The application of the relevant accounting standards; and iv. The service period, Audit fee and any resignation or dismissal of the auditor, provided that the engagement of an Audit Partner shall not exceed five years, and that the particular audit partner is not re-engaged for the audit before the expiry of three years from the date of the completion of the previous term.	Complied	The Audit Committee made the following recommendations in relation to this section; i. That Messrs BDO Partners, Chartered Accountants were reappointed as the external auditors of the Company for the financial year 2017/18. The Committee made this recommendation on the basis that this Audit engagement has not exceeded the maximum term of 5 years. BDO Partners are also approved by the regulator to provide external audit services. ii. That the Central Bank guidelines issued to auditors are implemented, as and when they are issued, on an on-going basis. iii. In reviewing the application of the accounting standards in preparing the draft financial statements, it was recommended that quantitative disclosure for SLFRS 9, a new standard taking effect from 1st January 2018, be included. iv. As the audit assignment carried out by BDO Partners is in its fourth year of service, the Committee recommended that the existing audit partner continues. The Audit committee decided on the Audit Fee for the financial year 2016/17. The committee noted that no resignations or dismissal of the auditor took place during the Financial Year under review.
8.2(d) The Committee shall review and monitor the External Auditors' independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices.	Complied	The External Auditor's independence, objectivity and the effectiveness of the audit process, was monitored and reviewed by the Audit Committee, mainly focusing on relevant professional and regulatory requirements specific to the LFC sector. Messrs BDO Partners, Chartered Accountants have provided a declaration of their independence to the Audit Committee, as the Company's External Auditors for the FY 2016/17.
8.2(e) The Committee shall develop and implement a policy with the approval of the Board on the engagement of an External Auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines.	Complied	The letter of engagement of Messrs BDO Partners, Chartered Accountants clearly specifies their scope of work and steps to be taken to avoid any conflicts of interest to safeguard the auditors' independence and objectivity. Hence, Messrs BDO Partners did not provide any non-audit services to the Company for the financial year 2016/17. Refer page 213 of Section D.3.3 of the SEC and ICASL code for further details.
8.2(f) The Committee shall, before the audit commences, discuss and finalise with the External Auditors the nature and scope of the audit.	Complied	The Audit Committee met the External Auditor, Messrs BDO Partners, Chartered Accountants four times during the financial year 2016/17.The Committee finalised the nature and scope of the audit with the audit partner, before the commencement of the audit. Areas needing special attention and recommendations of the auditors were incorporated into the discussions, and were included in the audit plan.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
8.2(g) The committee shall review the financial information of the finance company, in order to monitor the integrity of the financial statements of the finance company, its Annual Report, accounts and periodical reports prepared for disclosure, and the significant financial reporting judgments contained therein.	Complied	The Audit Committee periodically reviewed the financial information of the Company in order to monitor the integrity of the Annual Report, Financial Statements of the Company and other financial disclosures. Necessary changes were made thereafter by the Finance Department to the Financial Statements and other information contained in the Annual Report, before submitting to the Board for their approval. The Committee has reviewed the Company's Annual Report as well as the Quarterly Financial Statements before submission thereof to the Board for approval.
8.2(h) The Committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the Auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary.	Complied	During the financial year 2016/17, the Committee met the External Auditors three times of which two occasions were without the presence of the Executive Directors, in order to discuss matters arising from the management letter issued for the past audit period and to discuss key audit observations and findings.
8.2(i) The Committee shall review the External Auditors' management letter and the management's response.	Complied	The Committee reviewed the management letter issued by the External Auditors for the financial year 2016/17 together with management responses to ascertain material concerns requiring the immediate attention of the Audit Committee towards resolution, in the presence of the Finance Director. The committee took up key concerns with management who undertook to resolve the matters and issues brought to their attention.
8.2(j) The Committee shall take the following steps on Internal Audit: i. Review the adequacy of the scope, functions and resources of the Internal Audit Department, and satisfy itself that the Department has the necessary authority to carry out its work;	Complied	The Audit Committee has reviewed and approved the Internal Audit Plan for the financial year 2016/17 presented by the Internal Audit Department and prepared on a risk based approach having reviewed and assessed the overall risks of the Company and the significant audit observations made during the previous year. The Internal Audit scope, functions and resources of the department were assessed by both the Company's own Internal Audit Division as well as by Ernst & Young Advisory Services (Pvt) Limited. It was decided to strengthen the Company's own Internal Audit team in the next few years to ensure adequate audit coverage was provided. Based on manpower planning requirements of the department, four recruitments were carried out to increase the bench strength of the internal audit function and to widen its scope.
ii. Review the Internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the Internal Audit Department;	Complied	The Audit Committee reviewed the findings of the internal audits carried out during the financial year 2016/17 and the evaluation made by the Internal Audit Department on the adequacy of the Company's internal controls and compliances. The Audit Committee met five times with the Internal Auditors and reviewed the full audit/ spot review reports. In order to review the adequacy of scope and the risk based approach, separate audit programmes were submitted by Ernst & Young and the Internal Audit division of the Company for the financial year 2016/17, which were approved by the Committee. Necessary corrective actions were taken by MI on the internal audit findings and recommendations that were made during the year under review.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
iii. Review any appraisal or assessment of the performance of the head and senior staff members of the Internal Audit Department;	Complied	The head of the Internal Audit Department as well as the senior staff members were appraised for their performance as usual in the annual performance appraisal conducted by the Audit committee. The annual bonuses and the annual increments of the department were decided purely on the quality of the audit findings and the timeliness with which the audits were carried out. The performance of the Ernst & Young Advisory Services (Pvt) Limited was also reviewed by the Audit Committee for the FY 2016/17. The Committee concluded that all required audit deadlines were met and that the quality of reports was satisfactory.
iv. Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function;	Complied	The services of Ernst & Young Advisory Services (Pvt) Limited were continued to be obtained by the Audit Committee in parallel with the Company's own Audit team, to ensure head office and the entire branch network was reviewed at least once annually. The level of resources allocated by Ernst and Young Advisory Services (Pvt) Limited was accepted by the Committee and no queries were raised.
v. Ensure that the Committee is informed of resignations of senior staff members of the Internal Audit Department including the Chief Internal Auditor and any outsourced service providers, and to provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning; and	Complied	No senior staff members of the Internal Audit Department or Senior officers from Ernst and Young Advisory Services (Pvt) Limited handling the Company's internal audit function, have resigned during the year.
vi. Ensure that the Internal Audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care.	Complied	The Company's internal audit function is independent as the Department reports directly to the Audit Committee. Messrs Ernst & Young Advisory Services (Pvt) Limited is an independent institution engaged in the provision of audit services and having the resources and expertise to handle internal audit services impartially with professionalism. They too report directly to the Audit committee and have access to the Board in the event any matters need to be brought to the attention of the Board.
8.2(k) The Committee shall consider the major findings of internal investigations and management's responses thereto.	Complied	Based on the reports submitted by the Internal Audit Department, the Audit Committee reviews and considers audit findings on internal investigations and the management's responses thereto. However, no such major audit findings have been reported during the year 2016/17.
8.2(l) The Chief Finance Officer, the Chief Internal Auditor and a representative of the External Auditors may normally attend meetings. Other Board members and the Chief Executive Officer may also attend meetings upon the invitation of the Committee. However, at least once in six months, the Committee shall meet with the External Auditors without the Executive Directors being present.	Complied	The Finance Director/CFO attended Audit committee meetings on invitation, in addition to the Head of Internal Audit of Ernst & Young as well as the Company's own Internal Audit Officers being present to discuss the Audit findings. The committee met with the external Auditors twice this year without the presence of the Executive Directors in keeping to their section.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
8.2(m) The Committee shall have: i. Explicit authority to investigate into any matter within its terms of reference; ii. The resources which it needs to do so; iii. Full access to information; and iv. Authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.	Complied	Terms of Reference of the Audit Committee. The Board approved Terms of Reference of the Audit Committee mandates explicit authority to investigate any matter within its purview and take necessary action thereto. Refer: Board Audit Committee Report, Page 284 for a summary of Terms of Reference of the Board Audit Committee.
8.2(n) The Committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities.	Complied	The Board Audit Committee met Seven (07) times during the financial year under review. The Audit Committee Report given on page 284 provides details on how the Committee records its decisions.
8.2(o) The Board shall, in the Annual Report, disclose in an informative way, i. Details of Audit Committee activities; ii. The number of Audit Committee meetings held in the year; and iii. Details of attendance of each individual member at such meetings.	Complied	The activities of the Audit Committee and meetings held during this period with participation status have been disclosed on page 190 in the Board committee table. Further information is disclosed in Section D.3 of the SEC and ICASL Code on the Committee's scope of activities. The Audit Committee Report for financial year 2016/17 is given on page 284
8.2(p) The secretary to the Committee (who may be the Company Secretary or the head of the internal audit function) shall record and keep detailed minutes of the Committee meetings.	Complied	The Company Secretary, Mrs S. Pethiyagoda functions as the Secretary to the Board Audit Committee, and she records and maintains minutes of all Committee meetings in sufficient detail.
8.2(q) The Committee shall review arrangements by which employees of the finance company may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the Committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the finance company's relations with the External Auditor.	Complied ☑*G4-57 & 58*	The Board has approved a Whistle Blowing and Corporate Fraud Policy, which was developed by the Internal Audit department, which enables the employees to, in confidence, report violations of laws, rules, regulations or unethical conduct routed through the whistle-blower channels so that necessary actions can be taken by the Committee. The investigation process is laid down in the "Whistle Blowing and Corporate Fraud Policy" document issued in 2013. The confidentiality of those reporting violations is maintained and they are not subjected to any discriminatory action. During the financial year 2016/17, no material matters were reported to the Human Resource Division necessitating investigation by Audit or any other assigned party.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
8.3 Integrated Risk Management Committee (IRMC) The following shall apply in relation to the Integrated Risk Management Committee: 8.3(a) The Committee shall consist of at least one Non-Executive Director, CEO and Key Management Personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The Committee shall work with Key Management Personnel closely and make decisions on behalf of the Board within the framework of the authority and responsibility assigned to the Committee.	Complied	The Integrated Risk Management Committee (IRMC) comprises one Non-Executive Director (1) acting as the Chairman, while three Executive Directors (3) including the Managing Director comprise the full committee. The Committee's main duties are supervising broad risk categories such as credit, market, liquidity, operational and strategic risk. Refer the Board Committee Matrix on Pages 190 to 192. The Corporate Governance Report provides additional information pertaining to the IRMC on page 281. The members of IRMC work closely with Key Management Personnel of the Company to assess situations which arise on day to day business, and make sound decisions on behalf of the Board within the framework of the authority and responsibility assigned to the Committee.
8.3(b) The Committee shall assess all risks, i.e., credit, market, liquidity, operational and strategic risks to the finance company on a monthly basis through appropriate risk indicators and management information.	Complied	The IRMC assesses all risks, i.e., credit, market, liquidity operational and strategic risks through appropriate risk indicators. IRMC reviews the risk reports submitted by the Manager Risk and Compliance, on a quarterly basis and in the event of such risks are exceeding the established risk tolerance levels as highlighted by the reports submitted to the committee, the IRMC takes prompt corrective actions to mitigate the negative effects of specific risks. Refer section 8.3 (a) above on scope and tasks handled by the Committee. Refer the Board Committee Matrix on Pages 190 to 192. Refer the Risk Management Report on Pages 243 to 267 on wider explanation on the Company risk management approach.
8.3(c) The Committee shall review the adequacy and effectiveness of all management level committees such as the Credit Committee and the asset-liability committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the committee.	Complied	The IRMC reviewed the effectiveness of the Management Committee; studying management information presented at weekly forums and also reviewed the effectiveness of the Assets and Liabilities Management Committee and the Credit Committee. The Assets and Liability Committee (ALCO) of the Company reviews and monitors the liquidity risk and the market risk based on the risk tolerance levels (risk limits) established. The Credit Committee revised the credit authority levels with prescribed credit approval limits to evaluate the customer applications based on the nature of credit risk and the amount of the facility. Refer: IRMC Report, on page 281 for the scope of the Committee and its activities during the year 2016/17. Refer the Risk Management Report on pages 243 to 267 for a wider explanation on the Company's risk management approach.

Direction Requirement (With Section Number of the Direction)		Compliance Status	Extent of Adoption
8.3(d)	The Committee shall take prompt corrective actions to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the committee on the basis of the finance Company's policies and regulatory and supervisory requirements.	Complied	The IRMC of the Company has determined risk tolerance levels which are updated on a timely basis considering the factors such as strategic objectives of the Company, changes in regulatory requirements, competitiveness in the business environment and future economic conditions. Each risk category in the risk profile of the Company has been reviewed against the risk tolerance levels by the Committee and recommendations have been made when specific risks exceeded Risk Appetite limits to the Board. This will trickle down to the management level through appropriate communication channels. In reviewing specified Risk Appetite limits set for credit and liquidity risk, actual risk levels were compared against such limits and reported to Committee by Manager – Risk and Compliance. Summary of variances are disclosed on pages 253,255,257,259 and 266.
8.3(e)	The committee shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans.	Complied	The Integrated Risk Management Committee met four times during the FY 2016/17 on a quarterly basis. Page 190 provides information on meetings held along with attendance records of the Directors.
8.3(f)	The Committee shall take appropriate actions against the officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the Committee, and/or as directed by the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka.	N/A	The Committee did not come across any material violations by staff in relation to a breakdown in internal controls, non-compliance with risk management procedures and not taking appropriate measures to avoid material risks during the financial year under review.
8.3(g)	The Committee shall submit a risk assessment report within a week of each meeting to the Board seeking the Board's views, concurrence and/or specific directions.	Complied	The IRMC submitted risk reports to the Board within 7 days of having conducted their meetings, detailing a summary of key risks identified for the period, specifying risk mitigating actions proposed by the Committee for the Board's approval. Accordingly, four (4) activity reports have been submitted to the Board for the financial year 2016/17.
8.3(h)	The Committee shall establish a compliance function to assess the finance company's compliance with the laws, regulations, directions, rules, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from Key Management personnel shall carry out the compliance function and report to the committee periodically.	Complied	The Company has established a compliance function to assess the Company's compliance with laws, regulations and regulatory guidelines. The compliance function is headed by a qualified Accountant in the senior managerial cadre who directly reports to the Integrated Risk Management Committee on the Company's compliance with laws, regulations, directions, rules, regulatory guidelines and internal controls. A compliance status report was prepared and tabled monthly through the Finance Director for the Committee's information purposes, and a total of twelve (12) status reports were submitted during the financial year 2016/17 under review.

Corporate Governance Report

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
9. Related Party Transactions		
9.1 The following shall be in addition to the provisions contained in the Finance Companies (Lending) Direction, No. 1 of 2007 and the Finance Companies.	Complied	Directions relating to the Finance Companies (Lending) No. 1 of 2007 and the Finance Companies (Business Transactions with Directors and their Relatives) Direction, No. 2 of 2007 have been complied as mentioned on page 114.
9.2 (Business Transactions with Directors and their Relatives) Direction, No. 2 of 2007 or such other Directions that shall repeal and replace the said Directions from time to time.	Complied ☑ G4-41	During the FY 2014/15, a Related Party Transactions Review Committee (RPTC) was formed under the chairmanship of Mr. S.M.S.S. Bandara which reviews all related party transactions including accommodations to related parties. No lending has been made to Directors of the Company as per the above Direction.
9.3 The Board shall take the necessary steps to avoid any conflicts of interest that may arise from any transaction of the finance company with any person, and particularly with those who shall be considered as 'related parties' for the purposes of this Direction.	Complied	The Related Party Transactions Review Committee (RPTC) met quarterly to review the related party transactions for any known conflicts of interest that arose in a given quarter. Any conflicts of interest are monitored by the Board through this review by the RPTC. The process of capturing information and reporting related party transactions was streamlined further during this period in accordance with the provisions of this Section and the Sri Lanka Accounting Standard (LKAS - 24) on - "Related Party Transactions" for purpose of internal and external reporting. Refer: Related Party Transactions Review Committee Report, Page 285.
9.4 The transactions with a related party that are covered in this Direction shall be the following: a. Granting accommodation, b. Creating liabilities to the finance company in the form of deposits, borrowings and investments, c. Providing financial or non-financial services to the finance company or obtaining those services from the finance company, d. Creating or maintaining reporting lines and information flows between the finance company and any related party which may lead to share proprietary, confidential or otherwise sensitive information that may give benefits to such related party.	Complied	The Related Party Transaction Policy provides for the procedure to ensure that related party transactions effected have been carried out on an arm's length basis, and does not engage in transactions with related parties in a manner that would grant such parties "more favourable treatment" as defined in this rule. The Committee reviewed related party transactions carried out during this year to ensure they were at "an arm's length". As planned, the Committee carried out these reviews on a quarterly basis. Required disclosures on related party transactions have been disclosed in the Notes to the Financial Statements, on pages 341 to 343 while, Pages 277 to 278 disclose information relating to Directors' Interests in Contracts.
9.5 The Board shall ensure that the finance company does not engage in transactions with a related party in a manner that would grant such party "more favourable treatment" than that is accorded to other similar constituents of the finance company.	Complied	The Company has not entered into any transactions in a manner that would grant the related party "more favourable treatment" than if dealt with an unrelated party. Please see section 9.3 above that refers to the "Related Party transactions" and "Directors' Interests in Contracts" disclosures.

Direction Requirement (With Section Number of the Direction)	Compliance Status	Extent of Adoption
10. Disclosures		
10.1 The Board shall ensure that: a. Annual Audited Financial Statements and periodical financial statements are prepared and published in accordance with the formats prescribed by the regulatory and supervisory authorities and applicable accounting standards, and that b. Such statements are published in the newspapers in an abridged form, in Sinhala, Tamil and English.	Complied	The Company complied with applicable LKAS/SLFRS and other regulatory formats prior to publishing its annual audited financial statements and interim financials. The Financial Statements also conform to other regulatory requirements including the Finance Business Act, the Companies Act and rules specified by the Colombo Stock Exchange. Financial statements of the Company for the year 2016/17 were prepared and published in accordance with the reporting requirements prescribed by the regulatory and supervisory authorities and applicable accounting standards. The Board ensured that the financial statements were published in all three languages to conform to the regulatory requirement of the interim publication format and the applicable accounting standards.
10.2 The Board shall ensure that at least the following disclosures are made in the Annual Report:		
10.2(a) A statement to the effect that the Annual Audited Financial Statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures.	Complied	The Statement on Directors' Responsibility given on page 279 provides an affirmation that the Annual Audited Financial Statements have been prepared in accordance with the applicable accounting standards and applicable regulatory requirements.
10.2(b) A report by the Board on the finance company's internal control mechanism that confirms that the financial reporting system has been designed to provide a reasonable assurance regarding the reliability of financial reporting, and that the preparation of Financial Statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.	Complied	The "Report by the Board on Internal Controls" stating the effectiveness of the Company's internal controls mechanism over financial reporting, given on page 286 in the Annual Report provides the required disclosure to comply with this section.
10.2(c) The External Auditors' certification on the effectiveness of the internal control mechanism referred to in sub-paragraph (2) (b) above, in respect of any statements prepared or published from the date of this Direction.	Complied	The External Auditors' certification on the effectiveness of the internal control mechanism over financial reporting was obtained for the financial period 2016/17. No significant matters needing attention were highlighted as per the Report. The External Auditors' Assurance Report on the effectiveness of the internal controls over financial reporting has been disclosed on page 287 in the Annual Report.
10.2(d) Details of Directors, including names, transactions with the finance company.	Complied	Director Information including their names and other details are provided on page 177 while their transaction details are disclosed under the "Directors Interest In Contracts" on pages 277 to 278 and in the "Related Party Disclosures" in the Notes to the Financial Statements on pages 341 to 343.

Corporate Governance Report

<table>
<thead>
<tr><th>Direction Requirement (With Section Number of the Direction)</th><th>Compliance Status</th><th>Extent of Adoption</th></tr>
</thead>
<tbody>
<tr><td>10.2(e) Fees/remuneration paid by the finance company to the Directors in aggregate, in the Annual Reports published after 1st January 2010.</td><td>Complied</td><td>The remuneration paid to Directors in aggregate is disclosed on pages 277 to 278 in the Notes to the Financials Statements.</td></tr>
<tr><td>10.2(f) Total net accommodation as defined in paragraph 9 (4) outstanding in respect of each category of related parties and the net accommodation outstanding in respect of each category of related parties as a percentage of the finance company's capital funds.</td><td>Complied</td><td>Total accommodation to related parties of the Company has been disclosed on pages 341 to 343 in the Notes to the Financial Statements.
The net accommodation granted to each category of related party is given below as a percentage of the Company's capital funds:
<table>
<thead>
<tr><th>Category of Related Party</th><th>Amount Rs. 000</th><th>% Against Company's Capital Funds</th></tr>
</thead>
<tbody>
<tr><td>Key Management Personnel</td><td>-</td><td>-</td></tr>
<tr><td>Associate Companies</td><td>-</td><td>-</td></tr>
<tr><td>Others</td><td>14,331</td><td>0.21</td></tr>
</tbody>
</table>
There have not been any related party transactions exceeding 10% of the equity during the financial year 2016/17.</td></tr>
<tr><td>10.2(g) The aggregate values of remuneration paid by the finance company to its Key Management Personnel and the aggregate values of the transactions of the finance company with its key management personnel during the financial year, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the finance company.</td><td>Complied</td><td>The aggregate value of remuneration paid and transactions carried out by Key Management Personnel are disclosed under "Directors' Interest in Contracts" on pages 277 to 278 and in the "Related Party Disclosure" in the Notes to the Financial Statements. As per the Company's classification, Directors solely come under the definition of Key Management Personnel for the provisions of this section.</td></tr>
<tr><td>10.2(h) A report setting out details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any non-compliance.</td><td>Complied</td><td>"The Annual Report of the Board of Directors" signed by the Directors given on pages 271 to 276 includes collective confirmation on the Company's compliance with applicable laws and regulations. In addition, the Statement of 'The Directors Responsibility for Financial Reporting' given on page 279 confirms the Company's compliance with regulations on financial reporting.</td></tr>
<tr><td>10.2(i) A statement of the regulatory and supervisory concerns on lapses in the finance company's risk management, or non-compliance with the Act and rules and directions that have been communicated by the Director of the Department of Supervision of Non-Bank Financial Institutions, if so directed by the Monetary Board to be disclosed to the public with the measures.</td><td>Complied</td><td>There were no other matters brought to the attention of the Company to be disclosed.</td></tr>
<tr><td>10.2(j) The external auditors' certification of the compliance with the Corporate Governance Directions in the Annual Corporate Governance Reports published from the date of this Direction.</td><td>Complied</td><td>External Auditors BDO Partners reviewed the Company's compliance status to CBSL Corporate Governance Direction. Accordingly, they have issued a certification in this regard for the financial year 2016/17.</td></tr>
</tbody>
</table>

Mercantile Investments and Finance PLC's Compliance Status to the Listing Rules of Section 7.6 and 7.10 of the Colombo Stock Exchange

Listing rule No. 7.6-Contents of the Annual Report at a glance

Rule No	Disclosure Requirement	Section Reference	Status of Compliance	Page Reference
7.6 (i)	Names of persons who held the positions of Directors during the financial year	Annual Report to the Board of Directors on the Affairs of the Company.	Complied	274
7.6 (ii)	Principal activities of the Entity during the year and any changes therein	Significant Accounting Policies	Complied	295 to 301
7.6 (iii)	The names and the number of shares held by the 20 largest holders of voting and non-voting shares and the percentage of such shares held	Investor Relations	Complied	113
7.6 (iv)	The Public Holding percentage	Investor Relations	Complied	112
7.6 (v)	The statement of each Directors' holding and Chief Executive Officer's holding in shares of the Entity at the end of the financial year	Annual Report of the Board of Directors on the Affairs of the Company.	Complied	274
7.6 (vi)	Information pertaining to material foreseeable risk factors of the Entity	Risk Management	Complied	243 and 244
7.6 (vii)	Details of material issues pertaining to employees and industrial relations of the Entity	Not Applicable	Complied	N/A
7.6 (viii)	Extents, locations, valuations and the number of buildings of the Entity's land holdings and investment properties.	Notes to the Financial Statements	Complied	325 to 333
7.6 (ix)	Number of shares representing the Entity's stated capital	Notes to the Financial Statements (Note 39) Investor Relations	Complied	339 and 340 112
7.6 (x)	A distribution schedule of the number of holders in each class of equity securities, and the percentage of their total holdings	Investor Relations	Complied	112
7.6 (xi)	Equity Ratios Market Value	Investor Relations Investor Relations	Complied	114
7.6 (xii)	Significant changes in the Equity's fixed assets and the market value of land, if the value differs sustainability from the book value	Notes to the Financial Statements	Complied	295 to 301
7.6 (xiii)	Details of funds raised through Public issues, Rights issues and Private Placements during the year	Investor Relations	Complied	114
7.6 (xiv)	Information in respect of Employee Share Option Plan and Employee Share Ownership Plan	Notes to the Financial Statements	Complied	275
7.6 (xv)	Disclosures pertaining to Corporate Governance practices in terms of Rules 7.10.3, 7.10.5 c. and 7.10.6 c. of section 7 of the Rules	Corporate Governance Report	Complied	240 and 241
7.6 (xvi)	Disclosure on Related Party Transactions exceeding 10% of the Equity or 5% of the total assets of the Entity as per Audited Financial Statements, whichever is lower	Investor Relations	Complied	114

Corporate Governance Report

Compliance Status to listing rules of section 7.10 of the Colombo Stock Exchange

CSE Rule No.	Requirement	Compliance Status	Extent of Adoption (FY 2016/17 update)
7.10	**Overall compliance position in relation to SEC 7.10 (Corporate Governance)**	Complied	a. The Company is in compliance with the corporate governance rules specified by CSE for all listed companies and also complies with section 7.10 requirements specified under this section. b. The Company has complied with CBSL Corporate Governance Direction No 03 of 2008. Compliance status is given on pages 217 to 238.
7.10.1	Non- Executive Directors of a Listed Company	Complied	The Board of Directors of the Company comprised of five (5) Non-Executive Directors out of ten (10) Directors at MI. The Company maintained a 50% composition of Non-Executive Directors on the Board, throughout this period, complying with this requirement.
7.10.2	Independent Directors	Complied	
	a. Two or one third of the Non- Executive Directors of the Board, whichever is higher, should be independent.		Of the five (5) Non-Executive Directors at MI as at 31st March 2017, four (4) were Independent Non-Executive Directors.
	b. Submission of a declaration of independence by Independent Non-Executive Directors as per prescribed format.		All Non-Executive Directors have submitted declarations to the Company as per the format provided in the CSE code on corporate governance for 2016/17 financial year.
7.10.3	Disclosures Related to Directors	Complied	
	a. Disclosure of the names of Independent Non-Executive Directors.		As per Section 7.10.4, the names of all four Independent Non-Executive Directors are mentioned on Page 204 of the Corporate Governance Section A5.5 of the SEC and CA Sri Lanka Code.
	b. In the event a Director does not qualify as 'Independent' against any of the criteria set out by section 7.10.4 of the rule but if the Board, taking account all the circumstances, is of the opinion that the Director is nevertheless 'Independent', the Board shall specify the criteria not met and the basis for its determination in the Annual Report.		No such circumstance has occurred during financial year 2015/16.
	c. Disclosure of a brief resume of Directors in Annual Report.		Refer: Corporate Governance, Pages 176 to 177 for Director Profile.
	d. Upon appointment of a new Director to its Board, the Entity shall forthwith provide to the Colombo Stock Exchange a brief resume of such Director for dissemination to the public. Such resume shall include information on the matters itemized in paragraphs (a), (b) and (c) above.		The requirement will be complied with, upon appointment of a new Director to the MI Board.
7.10.4	Criteria for Defining "Independence"	Complied	The eight criteria of defining independence stipulated in this section have been fulfilled by all four (4) Non-Executive Directors of MI.

CSE Rule No.	Requirement	Compliance Status	Extent of Adoption (FY 2016/17 update)
7.10.5	Remuneration Committee A listed entity should have a Remuneration Committee.	Complied	
	a. Composition of the Remuneration Committee.		Details of the remuneration committee is provided on page 282.
	b. The Remuneration Committee shall recommend the remuneration of the Managing Director of the Company.		Two (2) out of three (3) members in the Remuneration Committee are Independent Non-Executive Directors. The Board Chairman who is an Independent Non-Executive Director is the Chairman of the Remuneration Committee.
	c. Disclosure of the Remuneration Committee in the Annual report;		Page 208 section B.2.1 of the SEC and ICASL Code provides necessary information.
	» Name of the Directors serving in the Committee,		Names of Directors in the Remuneration Committee are provided on page 282.
	» Statement of Remuneration Policy,		Refer to the Remuneration Committee Report on page 282.
	» Aggregate Remuneration paid to Executive Directors and Non- Executive Directors.		The Aggregate remuneration paid to Executive and Non-Executive Directors is provided on pages 277 to 278.
7.10.6	Audit Committee A listed entity should have an Audit Committee.	Complied	
	a. Composition of the Audit Committee;		Refer Audit Committee Report, on page 284.
	» Audit Committee shall comprise of Non – Executive Directors, a majority of whom shall be independent,		The Audit Committee comprised of three of Non-Executive Directors, two of whom are independent.
	» One Non-Executive Director shall be appointed as the Chairman of the Committee,		The Chairman of the Audit Committee is Mr. S.M.S.S. Bandara, who is an Independent Non-Executive Director.
	» The Chief Executive Officer and the Chief Financial Officer of the listed Company shall attend Audit Committee meetings,		During the financial year 2016/17, the Finance Director (CFO) attended the Audit Committee meetings by invitation.
	» The Chairman or one member of the Committee should be a member of a recognized professional accounting body.		The Chairman of the Audit Committee is a Chartered Accountant, with years of experience behind him in the Financial and Auditing field, and is a partner of B. R. De Silva, Chartered Accountants.
	b. Functions of the Audit Committee.		Refer to the Audit Committee Report, on page 284 and section D.3.3 of the SEC and ICASL Code details.
	c. Disclosures in Annual Report;		
	» The Name of the Directors comprising the Audit Committee,		Refer Board Committee information table, on pages 190 to 192.
	» The Committee shall make a determination of the independence of the Auditors and disclose the basis for such determination,		Refer Audit Committee Report, on page 284 and section D.3.2 of the SEC and ICASL Code for disclosure in this regard.
	» Annual Report shall contain a report by the Audit Committee, setting out the manner of compliance by the Entity in relation to the Section 7.10 of CSE Listing Rules.		Refer Audit Committee Report, on page 284.

Corporate Governance Report

MI's Compliance Status with CBSL Rules, Directions, Determinations, Notices and Guidelines

The Company's compliance with laws and regulations with specific focus on CBSL Directions is reported by the Manager-Risk and Compliance to the Board. The information table which provides a status update on compliance with the regulations as at 31st March 2017 is uploaded on the official web site, www.mi.com.lk.

Submission of CBSL Web Returns

All required CBSL web returns were submitted by the Company on or before the due dates for submission. The information table is uploaded on web site of the Company on www.mi.com.lk

http://mi.com.lk/value-creation/governance-risk-management/

Returns Submitted as Per Prevailing Regulations for LFC Sector Organisations

The information table is uploaded in the MI website (www.mi.com.lk).

External Auditors' Certification

The services of the External Auditors were obtained to certify the contents stated in the Corporate Governance Report in relation to the Finance Companies (Corporate Governance) Direction No. 03 of 2008 and related amendments. External Auditors confirmed that the disclosures given are in order according to their report prepared upon on agreed procedures dated 12th September 2017.

S. Pethiyagoda
Company Secretary

Shehan Sandanayaka
Manager-Risk and Compliance

Saro Weerasuriya
Chairman

Colombo
12th September 2017

Risk Management Report of The Company

Risk Management Highlights for Financial Year 2016/17

- Some of the key risk management areas were incorporated in Risk based auditing approach. e.g.: - Liquidity Risk, Interest Rate Risk etc.
- As a result of monitoring the interest rates movements regularly, we were able to take productive measures to safeguard net interest margins.
- IT Steering Committee Terms of Reference approved by the Board.
- Improved the quality of the information content submitted to the Assets and Liability Management Committee (ALCO) to improve the quality of informed decision making.
- Analytical study of trends, emerging risks and challenges, which provided valuable insight in minimizing the gap between actual performance and targets including additional strategic actions to minimize and bring risk within tolerance and improved the effectiveness of management practice.

☑ G4-46

Integrated Risk Management Framework

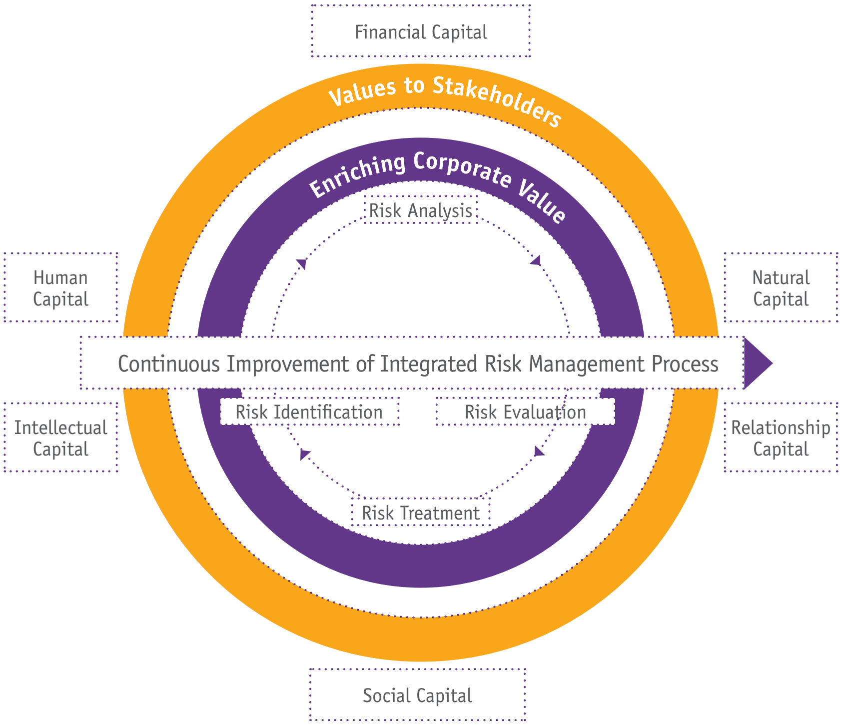
MI's Integrated Risk Management (IRM) Framework is well geared to support the organisation to effectively manage key risks associated with the provision of financial services in the non-banking financial services sector, paving the way to take on the emerging opportunities and challenges, to progress and gain market share. It ensures that the value of the six forms of capital we manage does not erode, assuring there is sustainable value constantly for MI stakeholders in a responsible manner, through the effective identification, monitoring, managing and controlling of various risks faced by the Company. The Board of Directors as well as the Senior Management is well aware of the significance of risk management, and stand firm in their responsibilities to set the tone at the top to ensure that an effective risk culture is nurtured across the organisation, in order to maximize stakeholder value. As a result, Risk Management has become an integral part of MI's business strategy each year. MI understands the importance of aligning Risk Management objectives of the Company in a manner that strikes an appropriate balance between risk and rewards.

The primary objectives of the framework are:

- Anticipating and mitigating risk events before they become a reality through early identification;
- Mitigating and managing risk in safeguarding the value of financial and non-financial capital integrating risk management at all levels of decision-making;
- Ensuring earnings stability and consistency;
- Protecting MI against possible losses in monetary terms and avoiding reputational damage; and
- Taking a proactive stance to future developments/changes.

The risk framework which sets out the Risk Appetite of the Company and encompasses the risk policies, key risk areas, methodologies to identify and manage risk, the allocation of responsibilities and segregation of duties between the three lines of defence, the governance and reporting structures that have been developed in line with all applicable regulatory requirements and international best practices is aimed at achieving the primary risk objectives outlined above. These goals are communicated and cascaded down the hierarchy of the Company. The Manager Risk and Compliance, who is the Risk Officer of the Company is responsible for driving the framework across the whole Company.

MI's Integrated Risk Management Framework



Risk Management Report of The Company

Risk Culture

A sound risk culture is a core element of the IRM framework and is deemed to be vital in building resilience for future sustainable growth within the overarching philosophy of prudence which we are known for. Risk Management is the responsibility of every employee acting as the first line of defence. In this regard, MI seeks to promote a culture where employees are aware of potential risks and threats related to their actions and work towards minimizing them by timely identification, escalation and exercising the appropriate risk mitigating or minimizing actions as specified in the risk management framework.

Risk Governance

The responsibility for ensuring that risks are identified, measured, managed and monitored on a timely basis and maintaining expected good governance standards in risk management ultimately lies with the Board of Directors. The Board discharges its duties through the delegation of authority and policies and procedures enacted by several Board appointed Sub-Committees, with the Integrated Risk Management Committee (IRMC) being the apex body for all risk related matters. Moreover, with the establishing of key Board Sub-Committees and management committees to provide the requisite oversight of the operational activities of the business and institutionalizing a comprehensive effective internal control mechanism, Corporate Management is soundly guided in the day-to-day management of the business. These measures seek to promote an awareness of risk and good governance in every area of the business, which reinforces a culture of compliance among all employees across the organisation.

MI's Three-Lines of Risk Management Defence

The foundation of MI's Risk Management framework is built on the 'Three Lines of Defence model (Refer MI's Risk Structure Encompassing Three-Lines of Defence on page 245) which segregates the duties and responsibilities between the staff who are the first line of defence, the risk officer who is the second line of defence and the assurance providers namely the internal auditors and external auditors who act as the third line of defence. The staff as the first line of defence being hands on with the management of the business is best equipped to identify early warnings and risks as part of their day to day management of operations. Timely escalation through the predefined channels of communication designed in the risk management framework lead to timely preventive actions being implemented to manage or mitigate the impacts from such risk identification.

The Manager Risk and Compliance in his role as risk officer is responsible for institutionalizing risk management framework across the organization and the provision of oversight on the management of risk and monitors the risk mitigation actions implemented by the management together with tabulating the corporate risk heat map and setting of Risk Appetite for identified risks under the oversight of the IRMC. The IRMC acts as the main channel that communicates the status of risk management actions and initiatives to both the Board and management and keeps the Board updated with the status of the risk heat map of the Company together with emerging risks in ensuring that the Risk Appetite defined is complied with in managing and bringing risks within tolerance.

The third line of defence, the Internal Audit function plays an important role of providing assurance to the Board, the Board appointed Sub-Committees and the management committees by testing and auditing compliance against the governance and risk management frameworks, the codes of conduct adopted by the Company and regulatory compliance and in assessing the effectiveness of the design and operation of internal controls and compliance with the applicable rules, regulations and laws governing the industry and the Company.

☑ G4- 46, 47

Risk Management Strategy

Risk management continues to increase in significance and complexity as technology, regulation and LFC sector operations evolve at a rapid pace. It is an integral part of the MI's value creation model that includes the six forms of capital, as we accept risk in the normal course of doing business, and the Company's stability and profitability are determined by how well we manage and mitigate risk. Significant resources are devoted to this critical function to ensure that it is articulated, communicated and understood by all employees, as it is a shared responsibility. It is a dynamic and disciplined function based on the triad of Credit risk, Market risk, Operational Risk, Compliance Risk and Reputational Risk etc. in order to face complexities and sophistication over time and also comply with stringent oversight by regulators.

As part of MI's risk management strategy, the Company adopts an on-going process of risk identification, which encompasses the assessment and measuring of risk levels and includes making improvements to existing risk mitigation practices on a case-by-case basis. MI's risk management process encapsulates a broad framework of policies and procedures and risk tolerance limits laid forth for management and staff to follow as a means of eliminating or mitigating risks at various levels. At the same time, the Company monitors risks on a continuous basis, in certain instances, comparing actuals against prudent norms to identify material deviations and also carried out stress testing to determine the impact of a particular risk

MI's Risk Structure Encompassing Three-Lines of Defence

Board of Directors
Key Risks Overseen - All Risks

Audit Committee
Key Risks Overseen - *All Risks*

Internal Audit Function
Key Risks Overseen - *Operational Risk*

3RD LINE OF DEFENCE - Independent Verification

This level involves the Internal Audit providing independent and objective assurance on the Risk Management /Compliance processes and practices in place, and has the authority to communicate with the External Auditors, Audit Committee and IRMC. Assurance is provided through;

- Internal Audit
- Anti-Fraud and monitoring
- Assessment of the robustness of the Risk Management and Compliance tools and techniques in place

Integrated Risk Management Committee
Key Risks Overseen - *All Risks*

Asset and Liability Management Committee
Key Risks Overseen - *Liquidity and Interest Rate Risk*

Compliance Function
Key Risks Overseen - *Regulatory Risk*

Credit Committee
Key Risks Overseen - *Credit Risk*

2ND LINE OF DEFENCE - Centralized Risk Management

This line of defence stems from the Centralized supervision initiated by the Risk and Compliance function to ensure the implementation of governance standards, frameworks and policies for each type of risk that the Company is exposed to, while ensuring consistency in Risk Management exercised across all areas. This is done through;

- Ongoing Formulation and implementation of the IRM framework.
- Review of Key Risk Indicators of the business units, products, processes, systems and reporting to the business units, management committees and IRMC, as required.
- Challenging the Risk and Control Self Assessments, brought to tackle inherent risks of business units.
- Independently identifying and assessing various risks the Company is exposed to, recommending action to maintain risks within the predetermined Risk Appetite levels.
- Overseeing the development of a risk-culture and its links with the anti-fraud framework issuing an independent 'Risk Opinion' for all Credit Appraisals, Operational Processes, Legal Agreements and New Products/ Systems.
- Conducting post disbursement reviews on loans and other credit facilities to ascertain compliance to covenants and ensuring maintenance of credit quality.
- Providing independent verification on the loan disbursement process and level of impairment carried out by the business units for individually significant borrowers.
- Independent monitoring of Treasury operations, adherence to Treasury limits, exposure to liquidity risk, interest rate risk, equity price risks and implementing or recommending appropriate actions to mitigate associated risks within Risk Appetite limits.
- Company-wide oversight of Risk Management, reporting and providing recommendations to IRMC.
- Monitoring Compliance with the Company's overall Risk Management framework.
- Other internal Compliance, regulatory compliance, regulatory reporting, and the application of Anti-Money Laundering measures.

Management Committee
Key Risks Overseen - *All Risks*

Corporate Management
Key Risks Overseen - *All Risks*

1ST LINE OF DEFENCE - Operational Line

Identification, management and reporting of both current and potential risks factors associated with MI's business are managed effectively as close as possible to the source of risk at operational level. Key Risk Management responsibilities for the business units' divisional level includes;

- Self-assessment and reporting of risks and control effectiveness
- Compliance with all policies and procedures
- Promoting a strong risk culture and awareness of risk elements through effective communication and training
- Identifying and implementing both proactive and reactive risk evaluation, monitoring, and controls, coordinating with Business Heads and Risk Management

Risk Management Report of The Company

under different variables. This provides MI the opportunity to assess the level of risk exposure that the Company faces and enables it to take timely counter measures. It also enables the Company to constantly keep appraising of the effectiveness of existing risk mitigation techniques, to stay in line with the evolving industry dynamics.

The Company possesses a strong risk governance structure at the core of its robust risk management framework. Risk governance of the Company is based on a three line defence system that ensures required accountability, independence and transparency of reporting, is maintained based on anticipated high standards. MI's three lines of defence in governing risks is depicted above and has been an effective counter mechanism against potential risks associated with the Company's type of finance business.

Risk Appetite

The overarching objective is to ensure that risks accepted are in line with the Company's Risk Appetite and strategic priorities and that there is an appropriate trade-off between risk and reward enabling delivery of value to key stakeholders. As an integral component of the overall strategy formulation process, MI's Risk Appetite demarcations provide measurable targets and tolerance thresholds across all material risk categories. This creates a framework where optimal growth options can be evaluated alongside the risks that impact sustainable performance. The Company Risk Appetite limits is set by IRMC on the guidance provided by the Board of Directors.

The main aim of setting a Risk Appetite is to ensure that risks are proactively managed and brought within tolerance as per the Board approved tolerance limits for each material risk category. Risk Appetite tolerance levels are set at different trigger levels, with clearly defined escalation requirements, which enable appropriate actions to be defined upfront and implemented as required. In cases where the tolerance levels are breached, it is the responsibility of the Manager Risk & Compliance to bring them to the attention of the Management and respective Board Sub-Committees, and the Board for necessary action.

The Board is tasked with reviewing and approving the Risk Appetite annually, to ensure alignment with the Company strategy, business environment and stakeholder requirements. Any amendments to Risk Appetite levels are arrived through discussions between Business Line Heads, the IRMC, other relevant Board Sub-Committees and the Risk officer and are thereafter subjected to Board approval.

Risk Policies and Guidelines

MI's Risk Management Policy is comprehensive, addressing the key risks managed by the Company, encompassing compliance with the regulatory requirements including the Finance Business Act No. 42 of 2011 and related acts, policies and guidelines issued by the regulators. This key Board approved document clearly defines the objectives, outlines priorities and processes and roles of the Board and Management in managing risk, shaping the risk culture of MI. The risk policy is reviewed by the IRMC, regularly depending on the regulatory and business needs. Guidelines facilitate implementation of policies and limits with operational detail including specification of types of facilities, such as processes, terms and conditions under which the Company will conduct business providing employees with the required clarity in their day-to-day work.

Monitoring and Reporting

Risk measurement, monitoring and reporting are the responsibilities of the risk management function which undergoes regular training programs to develop and refine their skills. They are well-supported by IT systems which enable extraction of data, analysis and modelling. Regular and ad hoc reports are generated for review by Senior Management, the Management Committees and the Board Sub-Committees such as the IRMC and Audit Committee and eventually the Board which rely on these reports for evaluating risk management and mitigation actions providing strategic direction and to make informed decisions. The reports provide information on aggregate measures of risks across products and portfolios which are compared to agreed policy limits, providing a clear picture of the amounts, types and sensitivities of the risks taken by the management. (These are discussed on page 247 which refers to each risk review)

☑ *G4- 45, 46*

The Board Role in Governing an Effective Risk Management Framework

The Board of Directors have the ultimate responsibility over managing risk and has delegated oversight responsibility to the IRMC which reports on risk at regular meetings of the Board. Risk is accepted, monitored and managed by the business units which report to the Managing Director (MD) forming the first line of defence. The Board is also responsible for setting the Risk Appetite for the business and the implementation thereon comes under the purview of the corporate management. Leadership has been provided by the chairman and the Board from the front, by establishing necessary Board Sub-Committees and other initiatives in delegating their responsibility expeditiously on management of risks related to the Company. These Sub-Committees monitor and report to the Board on various key forms of risks, with the intention of the discharging its obligations. Board members active participation in such Sub-Committee meetings on a periodic basis helps discharge Sub-Committees' duties effectively.

Role Played by The Committees in Risk Management

	Integrated Risk Management Committee (IRMC)	**Credit Committee**	**Audit Committee**	**Assets and Liabilities Committee (ALCO)**	**Management Committee**
Risk Reviewed	All risks	Credit Risk	All risks	Liquidity and Interest Rate	All risks
Reports Analysed	» Quarterly risk reports » Ad hoc risk reports	» Credit Appraisal reports » Credit Procedures	» Internal audit reports	» Quarterly ALCO assessment Reports » Additional reports on liquidity mismatch » Loan to value ratio report » Prudential ration reports	» Performance against targets and gaps report » Competitor analysis report
Key Risks Considerations	» Determined the appropriate Risk Appetite and MI's level of exposure. » Identified risks and monitored the management of key risks to reduce the likelihood of unwelcome surprises. » Periodically reviewed MI's approach to risk management.	» Reviewing and recommending high credit risk. » Monitored material value overdue accounts and proposed recovery actions. » Reviewed key credit policies.	» Evaluating the adequacy and effectiveness of the internal control system and setting up a process that provides continuous feedback. » Assessing management compliance to internal rules and external regulations. » Assessing quality of financial reporting.	» Assets and liability mismatch management. » Pricing and margin review. » Profit sensitivity to market variables.	» Profitability of core business operations. » Volumes gap assessments. » Asset quality considerations. » Core margin assessments.

Risk Management Report of The Company

	Integrated Risk Management Committee (IRMC)	Credit Committee	Audit Committee	Assets and Liabilities Committee (ALCO)	Management Committee
2016/17 Committee actions on Risks	» Approved major decisions affecting MI's risk profile. » Approved changes / improvements to key elements of its processes and procedures on MI's approach to risk management.	» Reviewing and approving high value credit. » Reviewed and revised the Credit Operational Manual.	» Followed up on material observations highlighted in the letter to the Management by the External Auditor during their statutory audit of the previous period. » Reviewed integrity of the financial information generated by the Finance Department in consultation with the CFO. » The Committee evaluated the accounting policies and accounting standards to ensure completeness and relevance to the operations of the Company.	» Recommended to obtain long term funding in order to bridge the maturity mismatch. » Base on interest rate sensitivity recommended margin improvement strategies.	» Re-strategised core business lines based on gaps. » Proactive measures in times of volatility.

Role of Corporate Management in Risk Management

MI's Corporate Management comprising of Senior Managerial Officers, have been entrusted with the task of implementing risk management policies and procedures within their functional areas and monitoring them on a continuous basis to ensure its constant application. MI's Corporate Management structure has been established with clear segregation of duties. The governance and risk management framework together with the control environment aides the Management in setting about their duties and executing their responsibilities with the expectation of the Board.

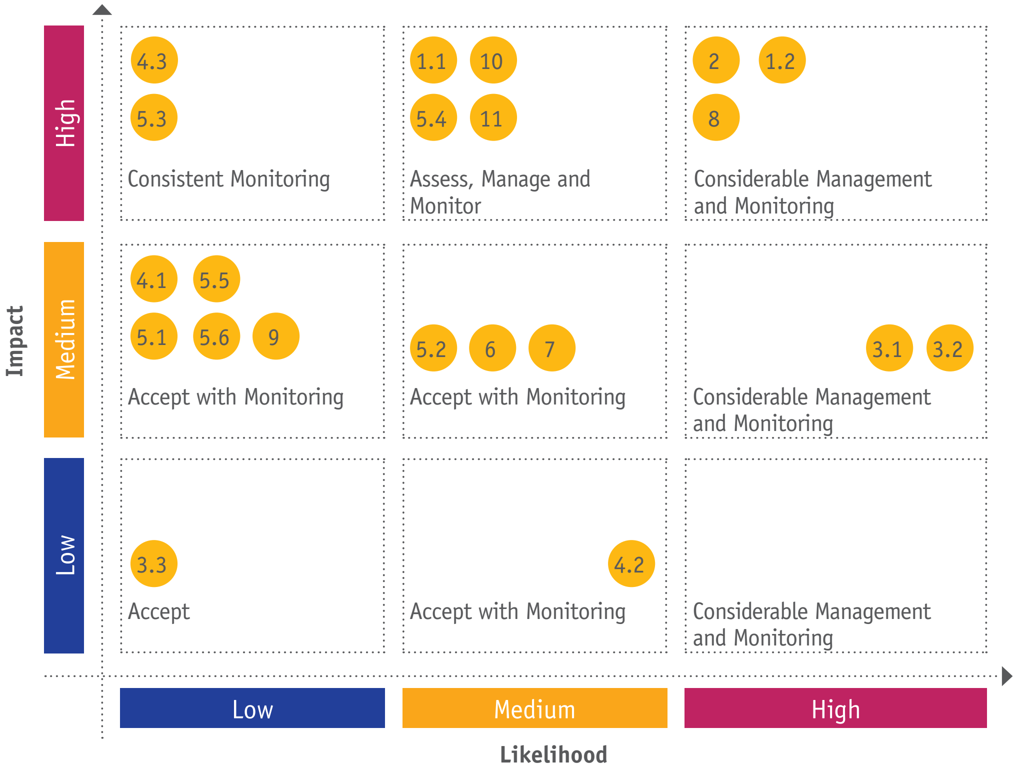
Divisional Heads have direct responsibility of ensuring that necessary risk assessments related to their departmental functions are done, including assessing the adequacy of prevailing risk management practices within the relevant divisions. Respective divisions are required to review existing processes and controls on a constant basis in the light of the changing environment, so that appropriate updating and improvements could be made to existing procedures and controls. Necessary procedural updating was effected, during the financial year, through addendums made to the Company's 'Procedure Manual', for the purpose of strengthening specific operations.

Risk Assessment

The IRMC with the assistance of Manager – Risk and Compliance carried out an ongoing risk assessment covering a broad range of risks associated with MI's finance business. A 'Risk Heat Map', was compiled, based on likelihood of occurrence and potential impacts, resulting as a consequence of each key risk, for the purpose of specifying different risk management strategies to tackle such risks. For this assessment, high, medium and low probabilities were assigned against each risk type, based on the likelihood of an event happening. Impact of each risk was then assessed by determining the financial and non-financial loss of each event. Based on the seriousness of each risk related impact, risk impact of each associated risk was thereafter classified as low, moderate and significant. Risks, where the likelihood and impact were high, were taken seriously for extensive management and monitoring (Red Zone). Accordingly, as the impact and the likelihood decreased, continuous monitoring was proposed.

(Refer Risk Heat Map on page 249.)

Risk Heat Map



ASSOCIATED RISKS

1. Credit Risk
    - 1.1 Default Risk
    - 1.2 Credit Concentration Risk
2. Liquidity Risk
3. Market Risk
    - 3.1 Interest rate Risk
    - 3.2 Equity Risk
    - 3.3 Foreign Currency Risk
4. Operational Risk
    - 4.1 Internal Control Risk
    - 4.2 Operating Environment Risk
    - 4.3 Unforeseen Natural Disaster Risk
5. Legal Risk
    - 5.1 Regulator Risk
    - 5.2 Insurers Risk
    - 5.3 Unknown Risk
    - 5.4 Suppliers Risk
    - 5.5 Borrowers Risk
    - 5.6 Stakeholders Risk
6. Technology Risk
7. Reputational Risk
8. Competitor Risk
9. Human Resource Related Risk
10. Compliance Risk
11. Strategic Risk

Credit Risk Management

Credit Risk is the risk of potential loss resulting from the failure of a customer/borrower or counterparty to honour its financial or contractual obligations to the Company. Credit risk may result in the loss of the principal amount and interest with adverse implications on profits due to the impairment provisions or write-offs of non-performing facilities.

For MI, this arises mainly from direct lending activities which are reflected On-Balance Sheet, such as leases, hire purchases and loan receivables. In light of the above MI has developed a well-structured risk management mechanism to manage this vital risk. Stringent credit policies and procedures have been established to counter credit risk, through a comprehensive credit manual, which is regularly updated for MI's requirements and rapid developments of the LFC sector.

The operational manual specifies clear policies, processes and procedures to follow when disbursing credit, until full recovery of dues covering all the stages of the credit cycle as depicted in the below Credit Risk Management Process Diagram. (Refer Credit Risk Management Process on page 250.)

Credit Origination, Approval and Risk Assessment

Our lending products, such as leases and loans are originated at Head office as well as at branch level. The credit proposals are evaluated based on the credit policy and guidelines of the Company. The credit evaluation takes in to account, the customer criteria including the loan purpose, vehicle/equipment security category, second-hand market value, and credit history and repayment capacity of the borrower. During the appraisal stage, the marketing officer who is identified to be the principal risk owner assesses the credit risk based on the Risk Appetite framework of the organisation.

As depicted in the Credit Approval Cycle on page 250, credit approvals are in line with the delegated authority limits set and are subject to an independent doer checker review by the next level of authority having a higher limit. The Board of Directors is the highest authority to approve credit facilities followed by the Credit Committee for higher value exposure. The Managing Director (MD), Director (Non-Board) Credit and Marketing, Assistant General Managers (AGMs), and Senior Managers at the head office have been delegated with authority to approve credit facilities. At branch level, the Branch Manager is the highest authority level to approve credit facilities subject to the prescribed credit limits. In addition to the delegated authority, manual controls require additional documentation verification about the customer and the asset which include requesting for a vehicle inspection report.

Risk Management Report of The Company

Credit Risk Management Process

Credit Disbursement and Collection Process

Inquiry	Application	Application Assessment	Approval	Disbursement	Collection
» Recording and follow up » Customer meeting » References	» Making operational evaluation of the credit request » Highlight key business risks » Obtain collaborative information on client background » Referring to credit reports such as CRIB Reports	» Request supporting documents » Decide facility structure » Completeness and plausibility review » Financial analysis » KYC review	» In-depth analysis of security provided » Valuations reports and evaluation of exposure » Bank Statements » Site visits » Authorization limits & higher level review of large disbursements.	» Release of disbursements centrally » Disbursement of money via a cheque » Strict personal identification check	» Regular periodic collection reports, NPL statics and arrears reports » Reminder callers and letters for default customers » Competent Recovery Officers » Special recovery task force » Impairment NPL monitoring

Credit Risk Control Mechanism

As part of this "credit review process", credit division ensures following key aspects are verified, prior to making the final disbursement.

- Physical verification of moveable and immovable assets
- Documentary evidence verification
- References
- Income sources
- Assessing past payment history i.e. CRIB report
- Assessing repayment capacity

In managing credit associated risks from a broader perspective, the Credit & Marketing Officer/ Credit Manager together with the respective AGM's are required to identify and evaluate the credit risk exposure connected to the credit proposal and is given authority to act within the designated authority limit, risk management policies and Risk Appetite levels which are defined. i.e. evaluation of the credit concentration level and existing market considerations.

Further, some of the credit policies and procedures are pre-defined at different levels; either by segregation of duties, setting authority limits etc. which mitigates credit operational risk through system driven embedded controls.

Credit Approval Cycle

Board of Directors

Credit Committee

Director (Non-Board)
– Credit and Marketing

AGMs – Credit
(Allocated to cluster)

Regional Credit Manager

Branch Managers

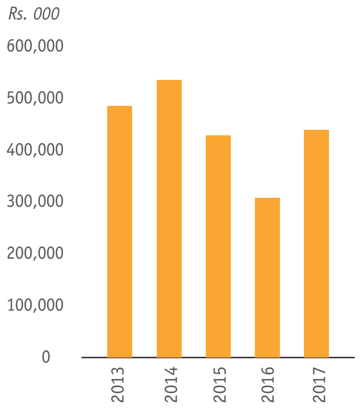
Branch Credit Officers

Credit Monitoring and Recovery

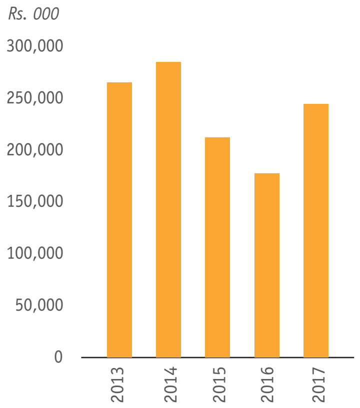
The Credit department of MI, measures and tracks the risk levels of the credit portfolio, undertake impact studies and detect early warning signals on any deterioration in the credit quality of the facility. Comprehensive management information reports are prepared on a monthly basis and submitted to the senior management. The IRMC provides required direction to the credit operations to maintain the credit risk indicators within the stipulated tolerance levels. The IRMC assesses the credit portfolio performance against risk tolerance levels and reviews the risk activity reports to capture negative trends in the credit portfolio on a quarterly basis.

In order to minimize credit exposure MI ensures that its lending is backed by adequate realizable security, in line with prevailing regulations on lending. The Recoveries Division works closely with the Credit and marketing division to ensure credit requirements are satisfactory and

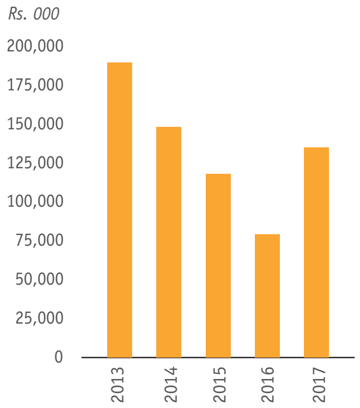
Non Performing Level-Overall



Non Performing - HP



Non performing lending - Lease



collections are received promptly. A vigorous collection monitoring system deployed by the recoveries division, tracks contracts moving into arrears on a daily basis and all past due borrowers are sent reminders to regularize any collection delays.

A special recovery task force is in place to speed up the recovery process for overdue problematic accounts. The credit recovery statistics are reviewed by the Credit and Recovery teams based on daily, weekly and monthly performance reports, which are taken up at weekly management meetings. Tougher recovery action is pursued in coordination with the legal department for problematic default accounts.

Credit Portfolio Monitoring Process Effectiveness

MI has developed a solid monitoring system to oversee more than 20,000 lending customers with the support of ICT systems and able credit staff.

Apart from system reports, CRIB reports, were obtained for borrowers and field visits carried to assess the creditworthiness of potential borrowers.

Compliance and Audit Review Over Credit Procedures

The organization's compliance was covered by the Internal Audit Department of MI in order to establish that credit policies and procedures are effective and have been complied with. The Director (Non-Board) - Credit and Marketing and respective cluster AGMs – Credit took the necessary follow up actions on all significant concerns highlighted in audit reports, under the supervision of the Audit Committee. Further, the Audit Committee appraised all material credit concerns and reported the findings to the Board. Credit review is part of the Audit teams full and spot audit process and this is an ongoing exercise. The Internal Audit department reported its findings to the Audit Committee and made recommendations to improve internal controls and processes.

Credit Concentration Risk

Credit Portfolio Concentration Risk arises when there is uneven distribution of Company loans to individual borrowers (Single name concentration), or in industry and services sectors and geographical regions (sectorial concentration). Concentration risk is assessed on the basis of quarterly studies on prospective different sectors in the market using available business publications and in-house research information. Through these studies, MI was able to identify early warning indicators such as high risk

Concentration of Credit Province Wise in 2016/17

Province	Hire Purchase 000'	Lease 000'	Other Loans 000'	Lending Outstanding 000'
Central	98,303	236,227	124,885	459,415
Eastern	89,094	523,896	78,279	691,269
North Central	253,591	743,529	310,455	1,307,574
North Western	492,566	932,515	546,444	1,971,525
Northern	876	10,574	2,545	13,994
Sabaragamuwa	291,263	803,362	709,016	1,803,641
Southern	417,380	1,105,485	1,334,459	2,857,324
Uva	63,590	107,479	60,583	231,652
Western	4,729,709	6,788,298	8,733,685	20,251,692
Total	6,436,371	11,251,365	11,900,350	29,588,087

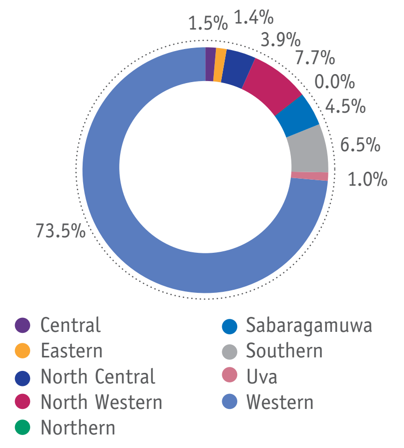
Risk Management Report of The Company

levels pertaining to specific industries or particular locations such as provinces that have higher credit risk than others. By diversifying the credit concentration, the Company was able to build a safety cushion, as any unfavourable movement in one sector could be offset by a favourable movement of another.

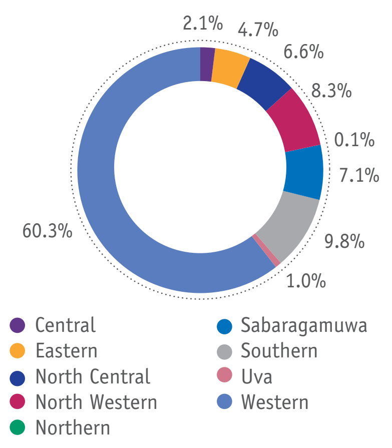
Concentration of Credit Sector Wise in 2016/17

Sector	Hire Purchase 000'	Lease 000'	Other Loans 000'	Lending Outstanding 000'
Agriculture	181,063	530,785	189,722	901,570
Commercial	1,171,772	2,000,610	2,858,940	6,031,322
Consumption	349,374	322,550	315,384	987,308
Finance	20,522	94,158	87,374	202,054
Housing and Property	83,290	77,134	351,783	512,207
Industrial	337,131	257,134	302,191	896,456
Services	3,234,030	5,899,188	5,699,060	14,832,278
Tourism	73,407	276,019	175,689	525,114
Others	985,782	1,793,788	1,920,208	4,699,778
Total	6,436,371	11,251,365	11,900,350	29,588,087

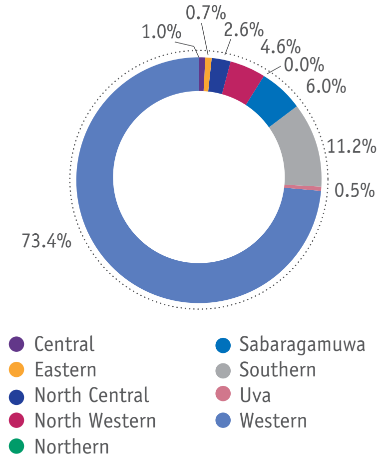
Hire Purchase Province wise Concentration



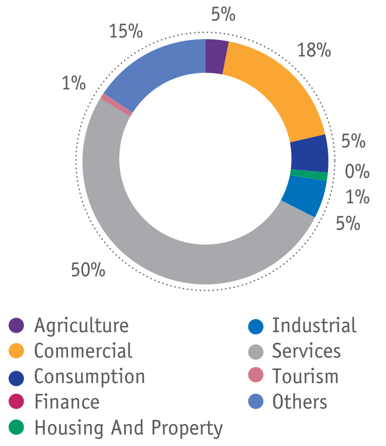
Lease Province wise Concentration



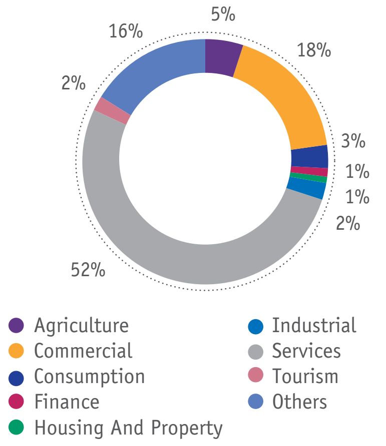
Other Loan Province wise Concentration



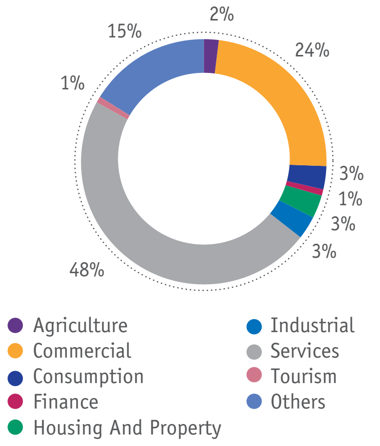
Hire Purchase Sectorwise Concentration



Lease Sectorwise Concentration



Other Loans Sectorwise Concentration



Credit Concentration Risk Assessment

Industry exposure on disbursement is prepared on a monthly basis to identify the level of exposure to each sector in the economy. This is reported to the IRMC on a quarterly basis. Additionally, the report on sector concentration is submitted to the CBSL on a monthly basis. The monitoring of credit concentration is an integral part of the credit risk monitoring process. Key ratio analysis and risk tolerance levels are used to measure and monitor credit concentration in the Company's lending portfolio. We also monitor the single name concentration and compliance to the prescribed single and group borrower limits by the regulator.

Strategies On Risk Mitigation

The concentration limits have been set under different criteria to support prudent portfolio management—industry/service sectors and product. The concentration limits are consistently monitored by the risk management department on a monthly basis and reported to the IRMC for their oversight and advice. To mitigate the location wise credit concentration risk MI's branch network has been diversified satisfactorily island wide. By further managing to open five branches in Thambuthegama, Avissawella, Gampola, Veyangoda and Wattala we were able to extend our reach beyond our existing locations.

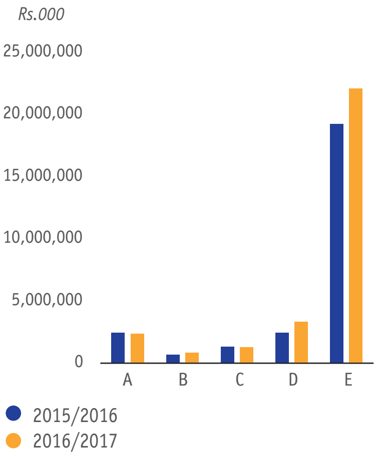
To improve the penetration level of low risk sectors and geographical areas in the market, the Company developed a strategy which will conversely reduce the exposure to high risk sectors, geographical areas and single group concentrations. Through the oversight of the Credit Committee, IRMC and the credit division reviewed and monitored the following key credit risks areas effectively.

- Limits on maximum exposure guidelines
- CBSL guidelines on single borrower limits and related party transactions

Ten Largest Credit as a % of Total Exposure

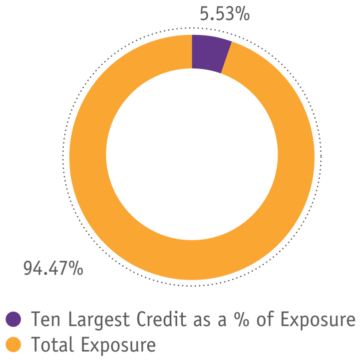
	2016/2017	2015/2016
Ten Largest Credit as a % of Exposure	5.53	7.19
Ten Largest Credit Rs. 000'	1,637,179	1,856,385
Total Exposure Rs. 000'	29,588,087	25,830,073

Credit Exposure by Counterparty



A-Corporate Over Rs. 10 Million
B-Corporate below Rs. 10 Million and above Rs. 5 Million
C-Corporates below Rs. 5 Million
D-Individuals Over Rs. 5 Million
E-Individuals below Rs. 5 Million

Ten Largest Credit as a % of Total Exposure



- Classification of borrower/sector
- Analysis of credit exposure limits against the actuals
- Exposure volume trend analysis

MI is within regulatory single borrower limits. A few large exposures have been adequately covered with prime collateral. There is a reasonable blend of both corporate clients and individuals in MI's credit portfolio and the Company is not exposed unnecessarily to risky lending sectors. (Refer the Credit Risk Appetite Criteria Table given below)

Credit Risk Appetite Criteria

Risk Appetite Criteria	Policy Range	Current Position as at 31st March 2017
Credit Quality		
Gross NPA%	Below 3.5%	6.9%
Provision Cover	Above 50%	46%
Credit Concentration-Sector-wise		
» Agriculture	Below 5%	3.05%
» Consumption	Below 4%	3.34%
» Services	Below 50%	50.13%
Single Borrower Limit (Individual)	As per Central Bank of Sri Lanka	11.66%

Risk Management Report of The Company

Liquidity Risk

Liquidity risk is the potential risk arising from the inability to meet obligations in a timely manner as and when they become due, mainly on account of mismatches between the maturities of the Company's assets and liabilities.

Non-banking Financial Institutions, such as MI, are vulnerable to liquidity and solvency problems resulting from asset and liability mismatches. This risk arises from mismatches in the timing of cash flows and therefore effective management of liquidity is important to ensure confidence and smooth operations to generate the required working capital, under any circumstance. Consequently, the primary objective of liquidity risk management is to assess and ensure availability of funds required to meet the obligations as and when they fall due both under normal and stressed conditions.

To strengthen oversight over liquidity management, we have formed a Board approved Asset and Liability Management Committee (ALCO), which is the main Executive Level committee mandated to oversee the Company's liquidity position to particularly ensure it is in line with the internal limits approved by the Board and reports directly to the Board on any deviations or findings.

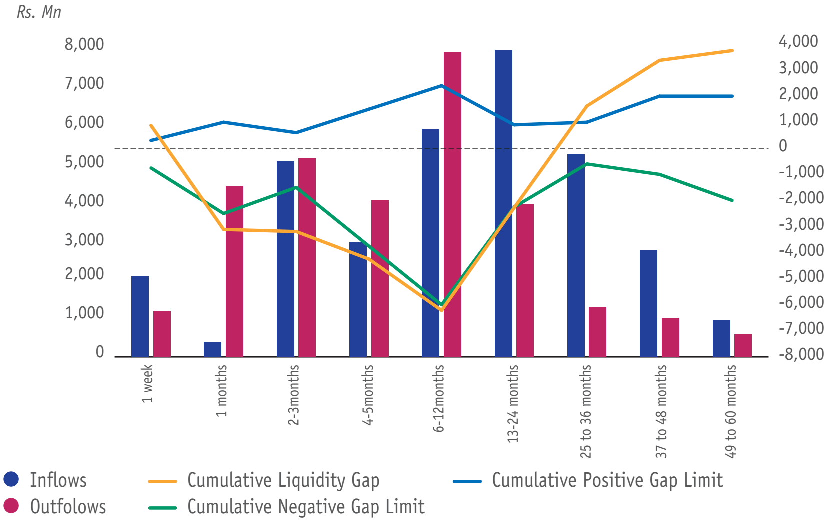
The Board Approved Liquidity Gap Limits are also used to ensure compliance with Central Bank regulatory requirements, and the Company's Risk Appetite. The impact arising from all strategic and medium term decisions taken by the Board and the corporate management on liquidity are also reviewed by this high level committee comprising key divisional heads.

Being a financially solid institution that has held strong liquidity positions right-throughout its long history, MI has access to diversified funding sources in addition to its core deposit mobilization business. The Board adopts a strict policy of managing its assets, and maintaining liquidity positions and as such has entrusted the Treasury division to monitor liquidity on a daily basis. We possess adequate cash and other liquid assets that include bank funding lines and access to money market instruments to meet any urgent funding needs as and when they fall due. Operational cash outflows arise from normal lending operations and also for meeting of overhead expenses, and other payments that include repayment of borrowed funds and outflows for investment. (Refer pages 293 to 294 for cash flow information).

The Company having built up a strong capital base is on a solid footing and has adequate flexibility to pursue its growth aspirations, and incur capital expenditure especially for branch expansion plans.

Apart from the Assets and Liability Management Committee's terms of reference on providing oversight over liquidity risk, MI has a Liquidity Management Policy which provides clear policy guidelines to the Treasury and relevant committees. Under the leadership of the Finance Director who oversees the treasury function of the liquidity risk measurement is carried out by assessing both the actual liquidity available and liquidity required on an expected cash flow basis. The actual liquidity available basis, evaluates the day to day funding requirements as well as the statutory ratio requirements which are monitored by supervisory committees. The expected cash flow basis assesses the forecasted cash inflows and outflows in different time buckets based on the maturity tenures of the assets and liabilities.

Liquidity Gap Analysis



Liquidity Risk Appetite Criteria

Risk Appetite Criteria	Policy Range	Current Position as at 31st March 2017
Net Advances to Deposit	Below 140%	168%
Liquidity Gap (Cumulative)		
» 1-7 Days Bucket	300 Million	880 Million
» 1 Month Bucket	(2,500 Million)	(3,110 Million)
» 2-3 Month Bucket	(1,500 Million)	(3,192 Million)
» 4-5 Month Bucket	(3,750 Million)	(4,247 Million)
» 7-12 Month Bucket	(6,000 Million)	(6,214 Million)

By contributing towards the deposit insurance scheme established by the regulator, there is an additional safety against liquidity risk. From a supervisory perspective, the Board provided stringent oversight by reviewing over the liquidity risk through its Sub-Committees the IRMC, the Audit Committee and the ALCO.

Sources of Funding

MI adopts a diversified funding strategy sourcing funds from multiple sources whilst considering the competitive environment, market conditions and regulatory aspects. Our objective is to maintain an optimum cost of capital through our funding mix at any given time. Deposits and term based borrowings are the largest funding sources of the Company. (Refer Financial Capital Funding Mix on Page 76)

Deposit Concentration

Deposit concentration is at a position of moderate risk on the risk heat map, where the treasury and the ALCO monitor the deposit portfolio and deposit movements periodically. The treasury monitors daily disbursements and collections to assess the impact to cash flow position.

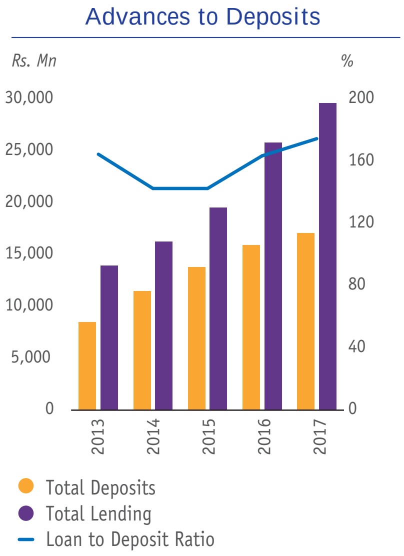
Contingent Funding Lines

The contingency funding plan provides guidance in managing liquidity in company specific or market specific stress scenarios. It outlines how assets and liabilities of the Company should be closely monitored, while emphasizing on the avoidance of a liquidity crisis. These procedures address unlikely but possible events in a worse cased scenario of short-term or long-term funding shortfalls, by reviewing the outcomes of forecasted funding needs as well as funding sources under different market situations such as aggressive asset growth or loan roll-over and rapid liability erosion or a sharp decline in deposits.

MI maintained adequate unutilised facilities to honour all cash commitments as and when they fell due, to mitigate against any form of liquidity risk. This ensured the availability of liquidity to meet our obligations and also to act as a buffer to support any temporary short falls in liquidity.

Liquidity Risk Mitigation

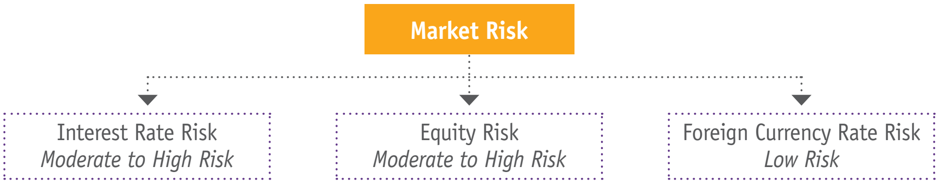
The Company as a practice maintains adequate margin in various liquid assets and access to diverse funding sources such as inter-bank market, wholesale and retail repurchase agreements, assets and investments held under the category of available-for-sale. Additionally, contingency funding agreements with commercial banks are in place, ensuring availability of adequate liquidity to fund our existing asset base growth whilst maintaining sufficient liquidity buffers to operate smoothly under varying market conditions including any short-term, medium or long-term market disruptions.



Risk Management Report of The Company

Market Risk

Market Risk is the likelihood of loss in earnings that could arise from the possible fall in value of investments or trading portfolios, as a direct consequence of changes in market variables such as interest rates, equity prices and foreign exchange rates. Most of MI's operations are subject to at least one or more elements of market risk. The process of managing market risk is underpinned by; the Asset and Liability Management Policy, the Investment Policy and the Treasury Policy.



Interest Rate Risk

Interest Rate Risk is the potential for losses resulting from the volatility in interest rates that impact rate sensitive products and the susceptibility of the future income and expense levels of a company to change, in line with movements in market interest rates.

MI is exposed to interest rate risk through a number of interest-bearing financial assets that are mainly grouped under Loans and Receivables, Finance Leases, Hire Purchase Receivables and Other Financial Assets.

As there is a direct core relationship between interest rate risk and interest spreads, Management was vigilant of the risk factors and took adequate measures to safeguard core spreads on a timely basis.

Given the continued rise in interest rates and the repricing effect impacting core spreads the treasury division pursued fixed rate longer term funding options, mostly opting for bank borrowings and securitisation. To secure favourable pricing, MI at times was compelled to secure floating rate borrowings capped to the AWPLR, but closely monitored interest rate movement impacting margins and the bottom line.

Management of Interest Rate Risk

Despite upward movements in interest rates continuing to be influenced by monetary policy changes that increased the interest paid on deposits and borrowings for the industry, the treasury negotiated favourable rates when raising short-term funds and thereby, managed to reduce the overall interest cost.

Apart from the resulting pressure exerted on our core margins, interest rate fluctuations continued to also impact;

i. our ability to canvass deposits and grant loans

ii. the fair values of financial assets and liabilities and

iii. average duration of mortgage backed lease and hire purchase portfolios and other interest earning assets.

In tandem with borrowings, deposit mobilisation played a vital part in shaping MI's funding costs, minimising the impact from rising interest rates. Depositors preferred the short term tenures in placing term deposits, on account of the possibility of a further increase in interest rates. MI on the other hand, was conservative in attracting high cost deposits of longer term and hence continued to meet the increasing demand for short term Fixed Deposit and Savings products. Further, we emphasize on building our retail deposit base as opposed to corporate depositors, through expanding our branch network as means of minimising the sensitivity to price changes.

Fixed and Floating Interest Bearing Assets and Liabilities as at 31st March 2017

	Fixed Rate 000	Floating Rate 000	Total 000
Interest Bearing Assets			
Placements with Bank	53,501	-	53,501
Financial Investments- Available-for-sale	4,587,048	-	3,893,551
Loans & Advances	11,448,668	-	11,366,577
Finance Lease Rentals Receivable	11,084,331	-	11,093,954
Hire purchase Instalments Receivable	6,154,480	-	6,184,744
Total Interest Bearing Assets	33,328,028	-	32,592,327
Interest Bearing Liabilities			
Bank Overdraft	1,092,434	-	1,092,434
Bank Borrowings	9,027,699	938,138	9,965,837
Other Borrowings	200,000	-	200,000
Deposits due to customers	17,017,674	-	17,017,674
Total Interest Bearing Liabilities	27,337,807	938,138	28,275,945

The Interest Rate Risk was monitored by the Board through the IRMC which was responsible for formulating policy including setting parameters and Risk Appetite limits.

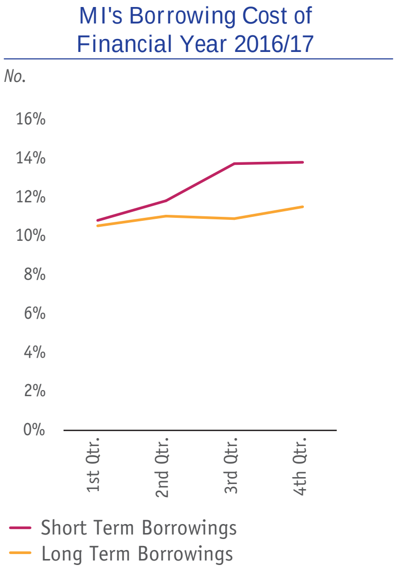
ALCO is the principal Management Committee responsible for monitoring Interest Rate risk exposure and initiating appropriate action plans to optimize overall market risk exposures within the defined Risk Appetite. The ALCO reviewed the current interest rate environments and the movement of key interest rate indices such as the Average Weighted Prime Lending Rate (AWPLR) and rates of government securities; and thereby, advised treasury on the organization's competitive lending rates and deposit rates, and regularly reviewed MI's interest rate risk and initiated appropriate action to minimise overall interest rate risk exposure within the Company's Risk Appetite limits. Maturity gap analysis was prepared considering interest rate sensitive assets and liabilities which enabled the committee to assess the impact on net interest income resulting from interest rate movements in the market. The net interest position and the maturity gap were evaluated on a monthly basis.

The treasury division independently monitors, measures and analyses exposures as per the comprehensive limit framework pertaining to treasury transactions. The treasury division remained responsible to manage funding and optimize pricing in keeping with the market rates and expected trends and was the manager of MI's total interest rate structure for its deposits and lending business on an ongoing basis.

As part of the Management Committee's scope, MI's interest rate structure was monitored closely against market trends, through which the Management was able to forecast interest rate cycles and resulting concerns to take timely decisions.

Interest Rate Risk Appetite Criteria

Risk Appetite Criteria	Policy Range	Current Position as at 31st March 2017
Interest rate 1% +(1%) Impact on Profitability (Million)	<50	62.29
Net Interest margin	>8%	7.42%



A comprehensive analysis was carried out by the Manager Risk and Compliance on the fluctuating interest rate to decide on the risk exposure and to assess the impact on net interest income. Ad hoc reports were also submitted to ALCO under the guidance of the Chief Financial Officer (CFO), who reviewed reports on MI's funding position, profitability levels, economic fundamentals, current trends.

In tandem the ALCO assessed the potential contribution of basis risk towards interest rate risk by monitoring movements in indices such as the AWPLR and rates of Government securities thereby, making appropriate decisions to re-price or rebalance the portfolios, as necessary, and carried out rate shock analysis, taking note of the upward movement to review the impact of interest rate change to MI's bottom line. These interest rate risk indicators were reported to the IRMC on a quarterly basis for their review. By having a strict monitoring system, the Management maintains the Company's interest rate risk at moderate levels despite the likelihood of occurrence being high.

Equity Risk

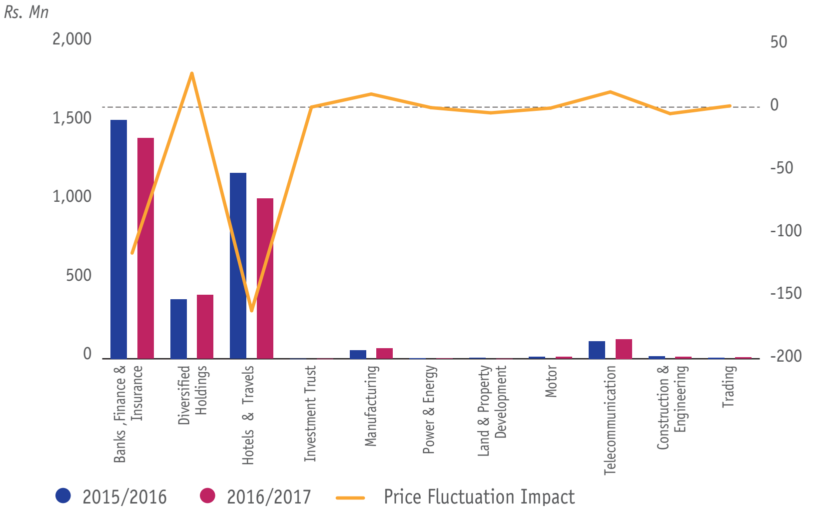
From MI's perspective, equity risk refers to the potential losses that may arise in the equity investment portfolio owing to adverse movements in value of equity prices.

The stock market indices tend to decline due to multiple reasons, including deterioration in investee company performance or net asset value and impacted by investor sentiment and macroeconomic policy decisions.

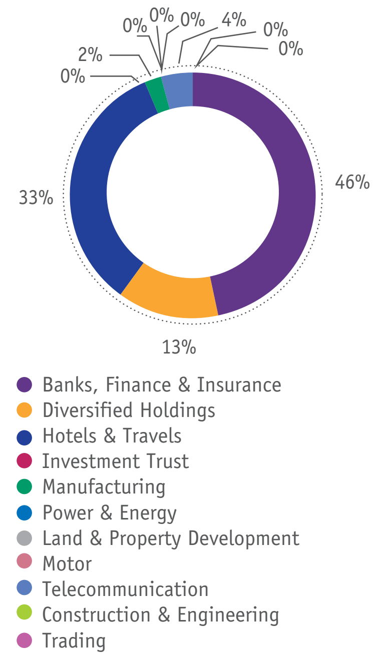
The persistent fall in share prices and the bearish nature of the stock market continued to impact the significant equity portfolio held by the Company. In this light Management monitored share price movements closely and remained passive in purchasing additional equity and focused on optimizing the realized gains on equity. The Company's accounting policies ensure that we reflect investments in shares at fair value recognizing any realized gains/losses through the profit and loss and unrealized gains/ losses through equity. Under the financial risk note in Page 357, we have analysed the potential impacts to share prices and its effect on profitability / equity based on pre-defined percentage movements in share prices of relevant shocks. The Board approved investment policy offers a comprehensive guideline for the management of equity risk within the specified Risk Appetite levels.

Risk Management Report of The Company

MI's Equity Investments Market Price Fluctuation 2015/16 vs. 2016/17



Sectorwise Equity based Investment Portfolio



Given the material value of the equity portfolio which amounted to Rs. 3 Billion as at 31st march 2017, and despite the portfolio being diversified through investments made in a range of sectors, MI remained vulnerable to equity risk especially with the continued volatility in share prices movements during this period. The capital market remained volatile due to outflows in foreign investments and changing economic policy. Owing to this, we executed stress testing on our equity portfolio based on possible downward conditions (Refer page 267 for equity stress testing results).

Despite possessing a well-diversified equity portfolio, mostly in blue chip companies, the persistent volatility and drop in share prices impacted the fair value of equity investments. MI's share portfolio had significant investments in the hotel, banking, and finance and insurance counters which are bound to appreciate in the future due to the existing development phase of the Sri Lankan economy. We reviewed capital market analysis reports, the returns realized from the equity portfolio due to movements in stock market and resulting fair value impacts and decided to hold most of the portfolio until the market revives.

Foreign Currency Risk

Foreign exchange rate risk relates to the losses from adverse exchange rate movements during a period in which the Company has an open position in a currency.

During the period under review, no foreign loans were raised nor were there any transactions entered in foreign currencies by the Company. The risk arising from movements in the exchange rate does not impact MI directly and is deemed an insignificant risk for the Company.

Operational Risk

Operational Risk is the risk of losses stemming from inadequate or failed internal processes, controls, people and systems, or from external events such as natural disasters, social or political events.

This risk is inherent in all MI products and processes and our objective is to control it in a cost-effective manner. We have designed and institutionalized various internal controls to detect possible human errors, fraud, faulty internal processes and systems, non-adherence to procedures and non-compliance with regulations.

A Company-wide effective internal control system is in place, requiring all staff to adhere to set policies and procedures related to various processes of the value creation process of the Company. To ensure clarity in required practices, the Company has developed a comprehensive procedure manual covering all key functions. We recognize that operational risk is inherent in all business activities and can bring unprecedented losses or damages to its business through direct or indirect financial loss, brand or reputational damage, customer dissatisfaction, or legal or regulatory penalties, if such risks are not objectively managed.

MI Operational Risk Management Framework

MI Operational Risk Management Framework

MI's operational Risk Management Framework is in accordance with the MI's Risk Management Policy and other related policies approved by the Board and applicable regulations, and it enables identification, measurement, monitoring, controlling and reporting of inherent and emerging operational risks.

Operational risk assessment is a process of identifying and evaluating events that could hinder corporate objectives. Such events can be identified both externally as well as within the internal environment.

Operational risk management techniques directly linked to people include segregation of staff duties, doer checker reviews, approval matrices with specified delegated authority levels, job rotation, staff training and development. These tools and controls are further reinforced by embedded ICT controls, the maintaining of documentation and backup of documents electronically.

Risk identification is the starting point of operational risk management and MI adopts several techniques to identify associated risks and this includes credit risk, liquidity risk, market risk and operational risk, etc. Once risk events are clearly identified, combinations of qualitative and quantitative assessments are carried out to evaluate the potential impact of such risks. Key risk indicators (KRIs) and audit findings are used to identify and assess these risk events. KRIs are categorised as per operational risk causes: process, people, systems and external events. The KRIs are objective risk measurements which allow trends to be monitored and can be used to anticipate risks in advance.

The responsibility to implement internal controls lies with respective heads of divisions for their operational activities while overall leadership for it stems from the Board. To ensure the effective functioning of embedded controls, respective divisions were expected to monitor such controls over time and make changes as and when needed to ensure that they are robust. The inherent nature of operational risk is such that it cannot be totally mitigated. We rely on ICT systems to support the manual controls with necessary automated embedded controls which require no human intervention and the provision of information for the purpose of analysis to minimize and/ or counter related risks. Numerous security controls have been in-built to core systems to eliminate possibility of unauthorized access, infiltration of data and system errors. Specific user limits have been established at various levels of the authorization process of transaction processing and a system of dual control has been implemented in core systems for all operational activities of importance.

Core systems provide management information including exception and ad hoc reports for the purpose of monitoring and analysing operational efficiency.

As a standard practice, daily back up is taken of the database and secured at an off-site

Operational Risk Appetite Criteria

Risk Appetite Criteria	Policy Range	Current Position as at 31st March 2017	Actions
» Internal Frauds	Below 3 Incidents	3	Comprehensive system of internal controls in place to mitigate potential operational risk.
» External Frauds/ Theft	Below 2 Incidents	1	
» Physical Assets Damages	Below 2 Incidents	Nil	Comprehensive Business Continuity Plan in place.
» Business disruptions due to System Failure	Below 2 Incidents	Nil	

Risk Management Report of The Company

location as a prudent measure in countering potential risk of system malfunction and corruption of data. We are fortunate to possess a team of in-house IT professionals having hands on experience in their field to manage software development and network administration. The team ensures system testing is made a must exercise when new modules are introduced or any material changes are made to existing modules.

Through the overall supervision of the Human Resource Management Division, human resource policy and practices have been put in to practice and any non-compliance with rules and procedures detected through Audits or otherwise is dealt with seriously.

The internal audit function acts as an early warning mechanism for Management, providing insights into any operational lapses or failures that may prevail so that proactive measures can be taken on a timely basis to avoid operational losses.

Numerous operational process improvements were made based on their recommendation apart from new and improved procedures introduced by functional management on an on-going basis.

As part of its duties, the Internal Audit is responsible for the ongoing review of the operational processes through audit reviews held regularly at both the head office and at the branches. Internal Audit reports are directed to the Audit Committee and the Corporate Management to take pertinent actions. The Company assesses and responds to factors impacting operational risks by applying a broad-based approach that seeks to regularly monitor errors or operational failures and respond to them with solutions and improvements to internal procedures.

Business Continuity Planning (BCP)

The Business Continuity Plan (BCP) of the Company spells out potential large scale risks to operations and what needs to be done by employees in the event of a Company-wide contingency event occurring such as a fire, flood, tsunami etc. The BCP specifies a clear path the management should follow and strategies that need to be implemented to minimize potential impact from such disaster events. In addition, all new product developments and the design of new processes were generally routed through risk management, audit and compliance divisions for their sanction. Appropriate sign off is obtained prior to implementing new or improved products. From a future stand point MI's strong capital base stands as a buffer against potential losses due to operational risks/contingency events if they were to materialise.

Operational Highlights for 2016/17

Part decentralization of Deposit operation but with sound Audit & oversight
Issuing of procedures for; » Deposit Function » Cashiering Function » AML Review (as per new Gazette requirements) » Credit Review (as per LFC sector developments)
Continued operational training to new comers and existing staff
Risk based audit approach and under coverage

Legal Risk

Legal risk can be defined as the risk of loss due to inadequate legal documentation of securities, penalties, fines, claims or customers filing law suits against the Company.

MI's legal risk can arise due to several reasons such as;

i. a defective transaction or;

ii. a claim (including a defence to a claim or a counter-claim) being made or some other event occurring which results in a liability for the Company or other loss (for example, as a result of a termination of a contract) or;

iii. failing to take appropriate measures to protect assets (for example, intellectual property) owned by the Company; or

iv. change in laws and regulations. Hence, there is an immediate need to deal in financial transactions with higher scrutiny in a highly regulated finance industry.

Regulatory changes would result in additional cost of compliance, may limit the type of financial services and products that could be offered in the market and in certain instances increase chances of competitors capitalizing on one's own offerings. Legal risk is managed carefully to avoid undue impact to business financially and to avoid damage to reputation that could lead to loss of confidence.

To tackle associated risks therefore, MI conducts a detailed legal risk assessment of our business across each of the following areas

- Regulator Risk
- Insurers Risk
- Unknown Risk
- Suppliers Risk
- Competitors Risk
- Borrowers Risk
- Stakeholders Risk

The Board, Corporate Management and all staff are required to understand the nitty-gritties involved in MI's operations and to apprise themselves of prevailing laws and regulations that change constantly. Employees are required to be conversant with regulations related to their daily work and are continuously trained to update their knowledge on changes in statutes, regulations including changes in interpretation or implementation of statutes, regulations and policies for due compliance.

MI's Compliance functions day to day operation comes under the purview of the Manager Risk and Compliance, and together with the expanding Internal Audit function that is able to monitor MI's adherence status to prevailing laws and acts, rules and regulations. Material non adherences to laws are reported immediately to the Board via the Audit Committee.

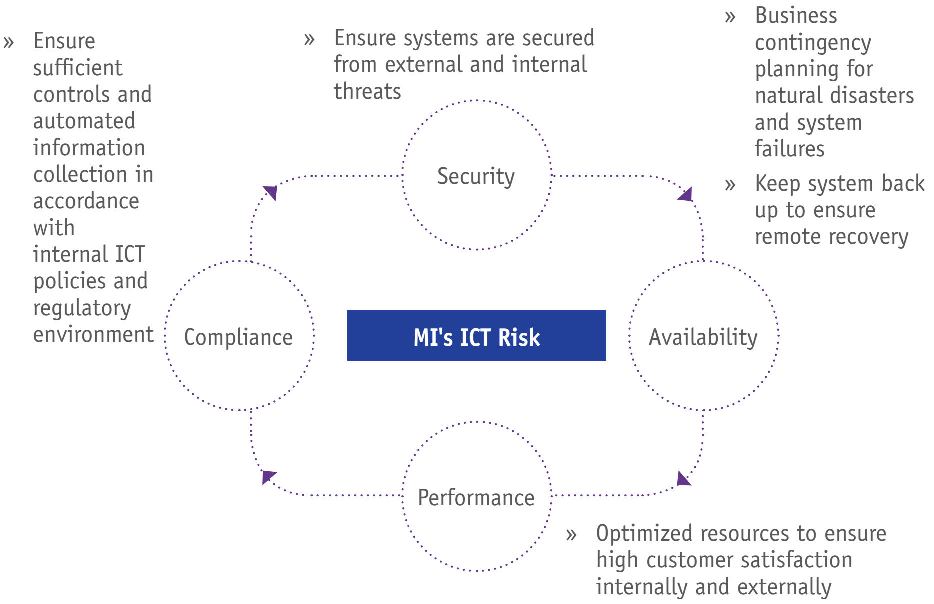
The Legal division prepares frequent management information reports for the Management's review. Those reports highlight on any unenforceability of contracts due to incomplete documentation, any penalties and fines paid, and also details of law suits against the Company. When new laws are enacted and whenever existing laws are amended, the guidance and clarifications in interpretation is provided by the legal division. Legal advice is sought when finalizing customer agreements; additional clauses and changes to agreements, recovery proceedings and whenever regulations related to products and services are introduced or are changed.

Legal risks faced by the Company are managed by the legal department. The legal department is headed by AGM Legal and consists of experienced lawyers capable of handling legal issues. Required third party consultations are also obtained, whenever required, in order to safe guard the Company against any legal risk.

Technology Risk

For a service organisation like MI, this is defined as the business risk associated with the use, ownership, operation, involvement, influence and adoption of ICT within an organisation, ICT Risk is a key area of concern globally as threats continue to escalate in magnitude and audacity. Although technology enables and extends vast opportunities in providing the Company with an operating platform to launch its business initiatives, it also poses serious risks which needs to be identified and well-managed. Breakdown and failure of information systems and the use of obsolete systems will adversely affect the smooth operations of the Company. Use of obsolete technology will erode the efficiency of the business operations and ultimately, affect the good reputation nurtured over the years. ICT risk is a major component of operational risk, and ICT risk comprises of ICT-related events such as system interruptions, errors, frauds through system manipulations, cyber-attacks, loss of confidential data, inefficiency due to obsolescence in applications, lagging behind competition who have been early adopters of innovative technology such as digitization and the cost of failed system upgrades and implementations that could potentially impact the business as a whole. Our ICT system has evolved over the years to meet business requirements and is a home grown system that has been upgraded and integrated onto our business activities. The fully integrated network system supports on-going branch expansion and growing product range and other business requirements. To keep pace with rapid changes in the industry, MI is on the verge of implementing an advanced IT system,

Main Components of MI's ICT Risk Management Framework



Risk Management Report of The Company

which will entail standard ICT risk and fresh set of risks associated with a system migration. Management hopes to manage the implementation, with the support of the external vendor and expert consultants in the next financial year.

MI has in place structured Board approved ICT policies and procedures that include information system security policies to govern the ICT operating environment. These ICT related policies are reviewed annually and updated when changes are necessitated. System Audits are conducted by the External Auditors annually and also by special review teams and their reports are furnished to the heads of divisions and the Audit Committee for their follow. The said review process encompasses the identification and addressing of potential threats to our IT systems—hardware and software.

A dedicated, IT department is responsible for implementation of the ICT Risk Management Framework for MI, facilitating management of all significant IT risks in a consistent and effective manner across the organisation. Officers recruited to the ICT Division are technology savvy, having a good understanding of the systems operated within the Company and possesses the capability to grasp system issues early and have the experience to resolve them. Our specialized software developers have the necessary technical know-how and comply with software development standards including adoption of user requirement documentation, system testing, implementation of standards, user acceptance testing procedures as part of MI's ICT Policy framework. When selecting hardware for our core systems, we remain with reputable organizations for our purchases and sign up for maintenance agreements with them to cope with equipment breakdowns and malfunctions.

The FY 2016/17 saw the number of cyber-attacks directed at global financial institutions of all sizes growing, including several high profile attacks involving fraudulent fund transfers, data breaches, ransom demands and other hacks. As a key player in the LFC sector, MI too realizes that it is a likely target for cyber-attacks akin to any other organisation. In light of this growing sophistication and variety of cyber-attacks and the scale of their impact, the Company has made reinforcements to counter against this emerging IT risk category, a top management priority, with the ICT Risk Function giving more focus to cyber security strategies.

Reputational Risk

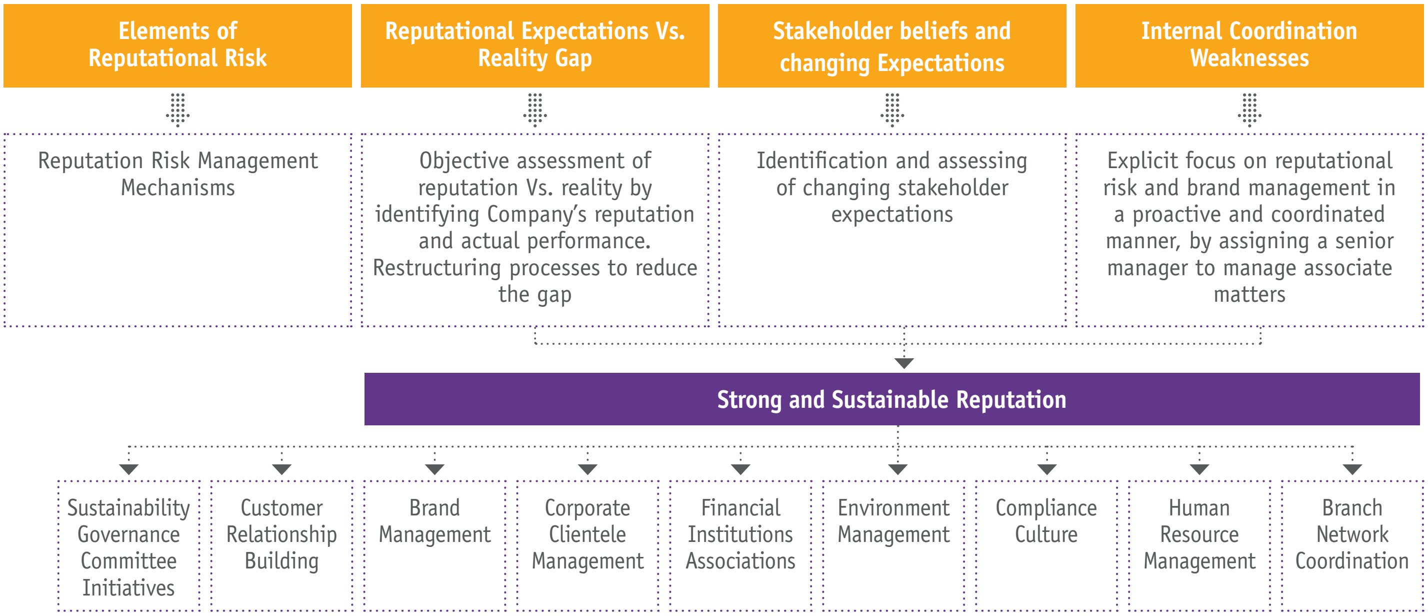
Reputational risks could arise as a direct or indirect consequence of all other key risks explained above, actually transpiring and negatively impacting the goodwill and brand name built up over a period of time, and this could have an adverse impact on MI's corporate brand. MI recognizes that reputational risk is driven by a wide range of other business risks that must all be actively managed on a timely basis. Accordingly, reputational risk is broadly managed through the systems and controls adopted for all other risk types such as credit, market, operational risk etc., which are underpinned by the code of conduct and business ethics. This risk could also arise when companies engage with other parties who do not abide by right standards and ethical business practices. Reputational damage will lead to companies experiencing deterioration in confidence of their customers which can directly impact business volumes and profitability. The Finance industry, particularly the LFC sector is highly sensitive to reputational risk, as investments are made mostly on public confidence and brand identity built up over the years.

For MI, reputational risk is broadly managed through various systems and controls implemented across the Company. Considerable amount of resources and efforts are placed in reviewing the business environment and MI's activities to ensure operations remain smooth and as anticipated without glitches. Our overarching business philosophy of prudence has led to culture compliance which continues have a positive impact on our people in preventing reputational risk and minimizing its impact. We have distinctively aligned our operations and practices especially front end processes to guide the Company to perfection. We provide greater autonomy to our managers to reduce lead times in completing transactions whilst placing a higher level of supervision and control over transactions that are material in nature. MI has developed a reputational risk management framework as depicted in page 263.

Through formal communication channels, customers can forward their grievances by informing branches, calling either the hotline number or through formal correspondence. Significant customer grievances are escalated from branch level to the branch operations department. An in-depth study is carried out on each grievance, liaising with the respective branch. The ICT department monitors the data link connection between the head office and the branches on a daily basis to ensure the continuous online real-time operations. MI's whistle-blower policy enables employees to inform of any malpractices anonymously and such information will be directly reported to the Audit Committee.

With clear job roles and duties at hand and by having an experienced and skilled team of financial experts, MI has the ability to respond well to the changes in markets and regulations governing the industry. Through Senior Manager Communications and Branding, a number of promotions and events were arranged at various locations to further enhance the brand image of the Company. He is entrusted with managing the intricacies of reputational risk for MI, in co-ordination with the heads of the core business divisions. MI remained focused on tackling pressing issues and has maintained a good track record in resolving

Reputational Risk Management Framework



any shortcomings that tend to arise as part of its daily operations. We adopt sound confidentiality policies and practices and use customer information responsibly. In safeguarding our reputation, we stuck to our fundamentals that inculcate practices of sound values and high ethical standards that are adopted across all our business activities. We resort to strict disciplinary action against individuals who fail to abide by set Company procedures and rules and adopt a zero tolerance approach in such instances and with regulatory non-compliance. To ensure there is no reputational damage from financial transactions in are dealings with our customers, we abide by the rules on Know Your Customer (KYC) and were able to implement the revised Board approved anti-money laundering policy document 2016, and which is implemented across all of our business lines.

Societal and Environmental Responsibility

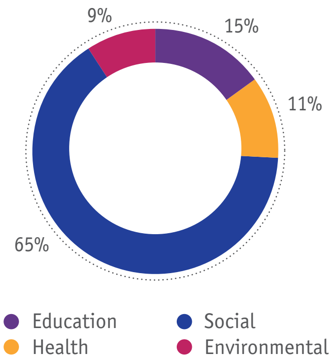
There was constant feedback generated from business locations on various societal needs and concerns with regard to the environment that were routed back to the Sustainability Governance Committee and Corporate Management for necessary review and action. A number of social and environmental worthy projects were initiated as explained in the section on sustainability that continued to underline MI's commitment to being a socially responsible corporate citizen, in keeping to its vision.

Refer:
Product responsibility - Page 106
Relationship Capital - Pages 94 to 115
Corporate Governance - Pages 182 to 242

Competitor Risk

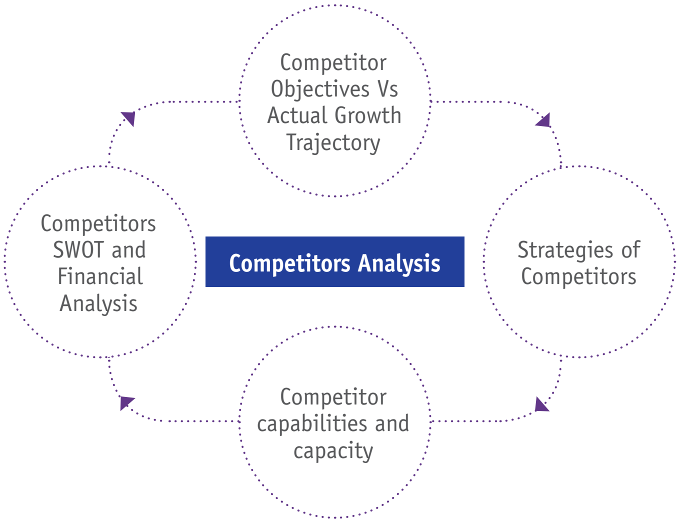
The growing demand for financial solutions and flexibility continues to propel the lucrative LFC sector. A large number of institutions compete aggressively in the industry to secure market share. The sector caters to a wide customer audience through a broad product range that has expanded from mere financing and deposit taking to tailor-made product and service offerings to satisfy diverse customer requirements. During the last decade the industry has become very sophisticated and competitive with technology being a driver of change and a disrupter of the existing status quo. Competition is further increased by the indirect completion from the Banking Sector who now carries out trading lending usually associated with finance company. In terms of deposit mobilization, availability of other alternative potential investment options such as the share market, corporate debt securities and investment in property have intensified the threat of substitutes.

Aspects of Community Investment



Risk Management Report of The Company

Competitors Analysis



MI has invested significantly in its operating platform in sustaining our core capabilities and critical success factors over the years; namely to maintain a superlative service and excellence in delivery. We have been able to provide tailor made solutions and affordable pricing. The opportunities to fine tune our operational practices over the years to meet with market expectations and challenges have improved MI's competitiveness.

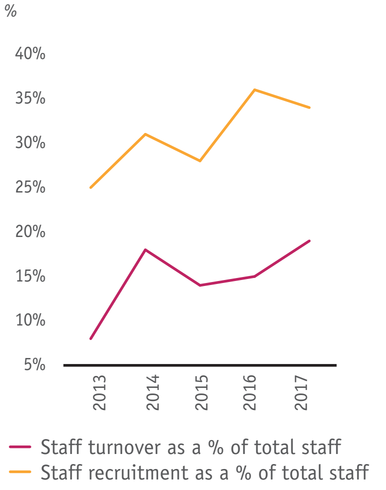
Mercantile Investments customer-centric approach and innovativeness coupled with competitive prices has made the Company a fierce competitor.

The use of advanced technology to execute core operations has improved our service and delivery times tremendously. Moreover, our unique human resource management style encourages a work life balance for our staff that remains motivated and productive. Having possessed a strong capital base built up for five decades, we are well geared to face competition and have the necessary financial capacity to respond to changing customer expectations and dynamic market conditions while pursuing strategic options and investment opportunities of our liking.

Human Resource Related Risk

People remain the most sought after asset in a service intensive industry, as a source of executing best in class service standards to maintain competitive advantage. Employees' talent, knowledge and experience underscore the organisational success. Attracting and retaining high calibre staff, who possesses the necessary experience and skills to perform duties is integral if MI is to pursue its goals and sustainable growth and profitability targets.

Staff turn over vs. Staff recruitments

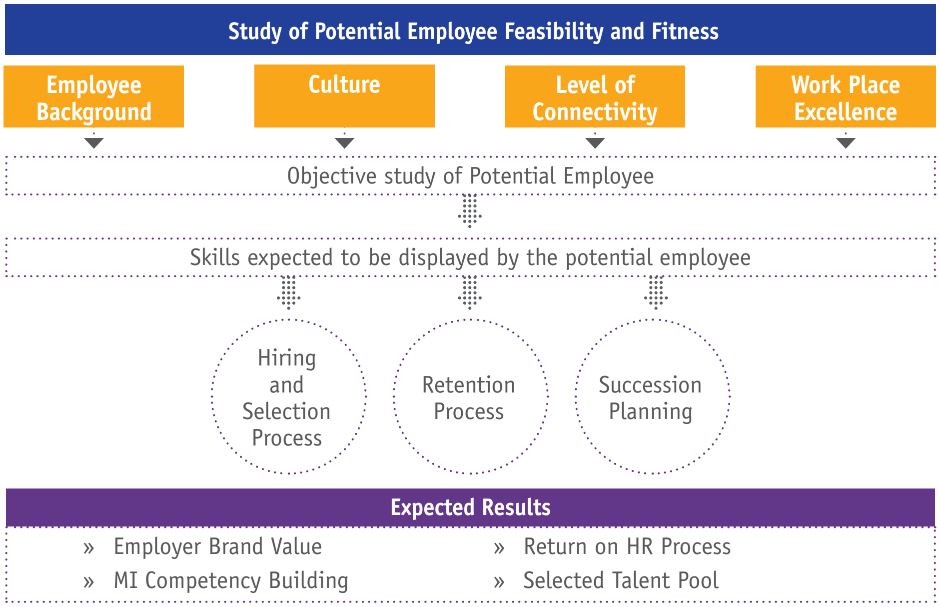


As most of MI's workforce has extended long service periods, losing the services of these experienced personnel could create a vacuum in meeting anticipated standards and may disrupt the smooth running of operations at least temporarily. In a competitive business backdrop, hiring qualified and experienced candidates and retaining top performers who are highly skilled and competent within the organisation is a challenging task. The turnover of trained and skilled staff in the industry especially the higher/middle management staff is on the rise and poses a significant risk in terms of talent retention in maintaining the competency of a Company and expected productivity and output.

Our focus is on talent sustainability, where we seek to attract, develop and retain employees with the capabilities and commitment needed for current and future organisational success. For us, talent sustainability entails an ongoing exercise and involves acquisition of skilled employees, learning and development, executive commitment and engagement towards succession planning, and performance management that is linked to reward and recognition. The Company conducts performance appraisals bi-annually and pays bonuses/incentives based on performance merits. Lack of effective training to address knowledge and skill gaps has a negative impact on talent sustainability. We at MI are focused on fulfilling the training needs, of our people and plan for succession, which in turn will help us retain high performing employees and ensure sustainable growth. As an integral part of our lifelong learning program, employees are provided with in-house and external training courses that support in developing their careers over time.

In motivating employees, we recognize valuable input of our staff by showing appreciation by offering competitive remuneration packages annually through salary increments, bonuses, special recognition awards and letters of

People Risk Management Process of MI



commendations. In improving staff morale, clear communication channels have been established between Management and staff in promoting concise dialogue that has helped to minimize misunderstandings. Training and development remained a key motivation tool that minimized the fear and anxiety faced by staff in addressing the challenges of a complex business environment that requires a high degree of technical skills. MI's low turnover levels suggest that we are a preferred employer especially because of the reputation that we hold, as a financially sound institution. Our financial stability continued to be a source of strength for our employees, affirming job security and career prospects for all dynamic individuals.

The Company always recognizes employees with potential to formulate a management succession plan and at times provide them with financial assistance for their higher studies as a capacity building measure. All staff members are free to meet their managers including the Directors at any time, to discuss their work related matters or discuss grievances.

MI has identified the importance of health and safety concerns of employees as a part of people risk management. Health and safety awareness programs are conducted periodically, addressing health issues ranging from work related stress, working patterns with computers and safety measures such as awareness on occupational accidents and work place safety especially at the MI Kohuwala workshop. The Company has established required safety measures to minimise work related injuries.

Strategic Risk

Strategic Risks are those that either affect or are created by strategic decisions. They could materialise due to internal or external factors and can cause reduction in shareholder value, loss of earnings, etc.

Strategic goals are determined through the corporate planning and budgeting process, and critical evaluation of their alignment with the MI's vision, mission and Risk Appetite, facilitates the management of strategic risk.

As part of the Board's role in directing and providing oversight over the operations, steps were taken to plan for the future and therefore, with the support of the Corporate Management, a comprehensive three year strategic plan was developed in 2015.

In order to evaluate the success of current strategies adopted and goals and targets set, the Board continued to monitor MI's financial and operational progress monthly. The Corporate Management weekly reviewed the KPI's/KRI's on a weekly basis to make informed decisions and realign performance through strategic actions when gaps were identified.

Each divisional head was asked to come up with their strategic actions that would achieve the objectives of the three year strategic plan and to evaluate the success of the ongoing implementation of the various strategies.

Functional heads monitored their KPI's and KRI's and proposed revised strategic actions if found to be required along with additional actions towards improving overall business performance and service levels.

The Board of Directors and Senior Management were encouraged to attend executive training programs on strategy to improve their knowledge and sharpen their skills and innovative thinking.

Engaging external consultants, to support in the development of the Corporate Strategy, was another initiative.

Risk Management Report of The Company

Compliance Risk

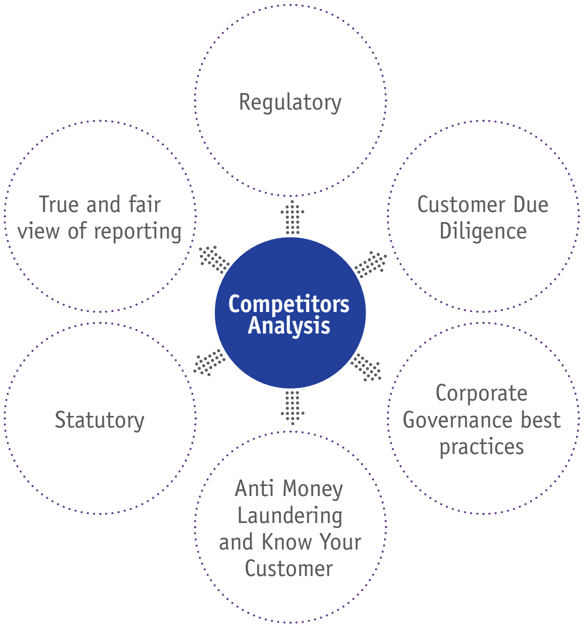
Compliance risk arises when there is a legal or regulatory sanction, causing financial losses or loss to a Company's reputation as a result of a Company's failure to comply with applicable laws, regulations, and carry out its business activities ethically and legitimately.

In evaluating compliance risk, timely reviews are carried out on a periodic basis to assess the extent of compliance with the regulations applicable to the Company. The Management and the Compliance Officer consistently review the changes in the regulatory environment to ensure compliance with all applicable rules, regulations and directives. In order to ensure that the required weekly reports are duly submitted, all computations are carried out on a daily basis and reviewed by the Compliance Officer (CO) before submission to the Central Bank of Sri Lanka and to other regulatory bodies.

A dedicated officer is designated as the CO, who is the Manager Risk & Compliance, who is accountable for independently assuring that operating business divisions are complying with regulatory requirements and internal controls. He oversees the compliance status of the Company with the relevant rules, regulations and directions set by the Central Bank of Sri Lanka, Securities and Exchange Commission of Sri Lanka, The Companies Act and other relevant agencies. The CO reviews the changes in regulations and takes necessary action to ensure that the Company is in compliance with the regulatory requirements. A sound regulatory monitoring mechanism is adopted to monitor reporting and compliance with all mandatory reporting requirements, with the intention of establishing a fully compliant corporate governance and risk mitigating culture.

In addition, the Compliance Officer reports to the IRMC on a quarterly basis. The Board with the assistance of the CO strives to institutionalize an organization wide compliance culture emphasizing characteristics such as integrity and honesty. Training and awareness programs were carried out during the financial year under review for corporate management and relevant officers to ensure that employees were apprised of MI's compliance requirements, policies and procedures and changes there to i.e. Anti-Money Laundering (AML) and Combatting the Financing of Terrorism (CFT). The Compliance Officer takes a proactive approach to promoting the compliance culture and considers the compliance function as a strategic partner for all the other core and support business divisions.

Compliance Risk Diagram



Risk Measurement Through Stress Testing

Stress testing is used as a primary means to assess MI's vulnerability to potential but plausible risk events and to determine how potential adverse developments may impact the adequacy of capital, liquidity, profitability and asset quality. In addition, stress tests also act as conduits from which the Company assesses changes in the risk profile and determines Risk Appetite tolerance levels.

Stress testing is conducted regularly for all major risk categories, while portfolio-specific stress testing is conducted quarterly for highly sensitive portfolios; mainly, lending, interest sensitive asset/liability and liquidity while for all other areas, stress tests are conducted as and when it is deemed necessary. Development, approval and review of stress tests are the responsibility of the IRMC.

Stress Testing

A fundamental role of risk management is to ensure organizations do anticipate for worst-case events early and strategies appropriately as they plan their path to success. Stress testing helps MI to evaluate potential impacts to its key financial variables due to adverse changes in business conditions or market variables so that we could be better prepared.

Base Data
(All figures are in Rs 000 and as 31st March 2017)

Total Risk Weighted Capital Adequacy Ratio (CAR)	14.26%
Capital Base	4,778,415
Risk Weighted Assets	33,517,976
Total Gross NPA	2,047,047
Equity Market Value	3,054,221
Deposit Liability	17,017,674
Gross Loans	29,543,573
NPL Ratio	6.92%

Stress Tests	Exposure Rs 000	Original Position 31st March 2017	Magnitude of shock		
			5%	10%	15%
		Total Risk Weighted Capital Adequacy Ratio (CAR) %	Revised CAR %		
A. Credit Risk					
Negative shift in Non Performing Advances *	2,047,047	14.26%	13.99%	13.73%	13.46%
B. Equity Price Risk					
Fall in stock market prices	3,054,221	14.26%	13.86%	13.47%	13.07%

Conclusion: No significant impact to capital adequacy due to shocks from credit risk or equity risk.

Stress Tests	Exposure Rs 000	Original Position 31st March 2017	Magnitude of shock		
			5%	10%	15%
		NPL %	Revised NPL %		
A. Credit Risk					
Negative shift in Non Performing Loans *	2,047,047	6.92%	7.28%	7.62%	7.97%

Conclusion: Despite the NPL being above the industry average, it will worsen if the shock level is increased. The large few NPL's comprises of 4% of total NPL of 6.92% and is fully collateral backed eliminating credit exposure.

Financial Reports

suc•cess•ful

adjective

1. *accomplishing an aim or purpose*
2. *having achieved popularity, profit, or distinction*

Synonyms

1. flourishing, thriving. 2. effective.

Financial Calendar

	2016/17
2015/16 Annual Report and Audited Financial Statements signed on	13th June 2016
53rd Annual General Meeting held on	14th July 2016
2016/17 Annual Report and Audited Financial Statements signed on	12th September 2017
54th Annual General Meeting to be held on	20th October 2017

Submission of the Interim Financial Statements in Terms of the Rule 7.4 of the Colombo Stock Exchange and as per the Requirements of the Central Bank of Sri Lanka

	2016/17 Submitted on	2017/18 to be submitted on or before
For the 3 months ended 30th June – (unaudited)	05th August 2016	15th August 2017
For the 3 and 6 months ended 30th September – (unaudited)	15th November 2016	15th November 2017
For the 3 and 9 months ended 31st December – (unaudited)	15th February 2017	15th February 2018
For the 3 months and year ended 31st March – (unaudited)	31st May 2017	31st May 2018

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Annual Report of the Board of Directors

Annual Report of the Board of Directors on the affairs of the Company and statement of Compliance of the contents of the Annual Report.

The details set out herein provide the information required by the section 168 of the Companies Act No 7 of 2007 and recommended best accounting practices.

1. General

The Directors of Mercantile Investments and Finance PLC have pleasure in presenting to the shareholders this report together with the Audited Financial Statements for the year ended March 31, 2017 and the Auditors' Report on those Financial Statements, conforming to the requirement of the Companies Act No 07 of 2007, Finance Business Act 42 of 2011 and the Directions issued thereunder.

Mercantile Investments and Finance PLC is a public limited liability company incorporated in Sri Lanka on 15 June 1964 under the Companies Ordinance No 51 of 1938 and re registered under the Company Act No 07 of 2007 and a licensed Finance Company under the, Finance Business Act 42 of 2011.

The ordinary shares of the Company are quoted on the Diri savi board of the Colombo Stock Exchange since June 2011. The senior unsecured redeemable debentures issued by the Company are also listed on the Colombo Stock Exchange. Fitch Ratings Lanka Ltd has assigned BBB- long term financial institution ratings respectively to the Company.

The registered office of the Company is situated at No 236, Galle Road, Colombo 03, which is also its Head Office.

This Report provides the information as required by the Companies Act No 07 of 2007, Finance Companies (Corporate Governance) Direction No 03 of 2008 and subsequent amendments thereto, Listing Rules of the Colombo Stock Exchange and recommended best practices on Corporate Governance. This Report was approved by the Board of Directors on September 14, 2017.

Section 168 of the Companies Act No 07 of the 2007, requires the following information to be published in the Annual Report, Prepared for the year under review (i.e., for the year ended March 31, 2017)

2. Review of Business

2.1 Vision, Mission and Corporate Conduct

The Company's Vision and Mission are given on page 32 of this Report. The business activities of the Company are conducted maintaining the highest level of ethical standards in achieving its Vision and Mission, which reflects our commitment to high standards of business conducts and ethics.

2.2 Reviews on Operations of the Company

The Company has established delivery points across all key regional hubs of the country. During the year, 5 new delivery points were added (5 in 2016), bringing the total number of delivery points in country to 36 at the end of 2017 (31 at the end of 2016)

A review of operations of the Company during the financial year and results of those operations are contained in the Chairman's Review, Managing Director's Review on pages 16 to 28 and Management Discussion & Analysis on pages 53 to 170 of this Annual Report

Segment wise contribution to revenue, results, assets and Liabilities is disclosed in Note 51 to the Financial Statements on pages 345 to 347.

2.2.1 Principle Activities of the Company

The principle business activities of the Company consist of finance leasing, hire purchase financing, term loan financing, fleet management, micro financing, share trading and mobilisation of deposits. There have been no significant changes in the nature of the principal activities of the Company during the financial year under review.

2.2.2 Associate Company

Company has a 26.12% (2016 – 26.12%) holding in The Nuwara Eliya Hotels Company PLC which is a quoted public company and involving in the business of hotelliering.Details of investments in associate is given in note 29 to Financial Statement on page 324 to 325 of this Annual Report

2.3 Financial Statements of the Company

The Financial Statements of the Company duly certified by the Chief Financial Officer and

	Information required to be disclosed	Reference to the Companies Act
I)	The nature of the business of the Company. together with any change thereof during the accounting period	Section 168 (1) (a)
II)	Completed and signed Financial Statements of the Company for the accounting period completed.	Section 168 (1) (b)
III)	Auditor's Report on Financial Statements of the Company and the Group	Section 168 (1) (c)
IV)	Any changes made to the Accounting policies during the year under review.	Section 168 (1) (d)
V)	Particulars of the entries in the Interests Registers of the Company during the accounting period.	Section 168 (1) (e)
VI)	Remuneration and other benefits paid to Directors of the Company during the period.	Section 168 (1) (f)
VII)	Total amount of donations made by the Company during the period.	Section 168 (1) (g)
VIII)	Information on Directorate of the Company during and at the end of the accounting period.	Section 168 (1) (h)
IX)	Separate disclosure on amounts payable by the Company to the Auditor as Audit Fees and fees for other services rendered during the accounting period.	Section 168 (1) (i)
X)	Auditors' relationship or any interest with the Company	Section 168 (1) (j)
XI)	Acknowledgment of the contents of this report/signatures on behalf of the Board by two Directors and the Secretary of the Company.	Section168 (1) (k)

Annual Report of the Board of Directors

approved by two Directors in compliance with the requirements of sections 151, and 168(1) (b) of the Companies Act No 07 of 2007 are given on pages 291 of the Annual Report.

2.4 Directors' Responsibility for Financial Reporting

The Directors are responsible for the preparation of Financial Statements of the Company to reflect a true & fair view of the state of its affairs. The Directors are of the view that Statement of Comprehensive income, Statement of Financial Position, Statement of Changes in Equity ,Cash Flow Statement, Significant Accounting Policies & Notes thereto appearing on pages 290 to 348 have been prepared in accordance with the requirements of the Sri Lanka Accounting Standards as mandated by the Sri Lanka Accounting and Auditing Standards Act No 15 of 1995 and the Companies Act No 07 of 2007.Further,these Financial Statements also comply with the requirements of the Finance Business Act 42 of 2011 and the listing rules of the Colombo Stock Exchange. The statement of 'Directors Responsibilities' appearing on page 279 of this Annual Report forms an integral part of this report.

2.5 Auditors' Report

Company's Auditors, Messrs BDO Partners performed the audit on the Financial Statements for the year ended March 31, 2017 and the Auditor's Report on the Financial Statements is given on pages 288 of this Annual Report as required by section 168(1)(c) of the companies Act No 07 of 2007.

2.6 Accounting Policies & Changes during the year

The Company prepared its Financial Statements for all periods up to and including the year ended March 31, 2017, in accordance with Sri Lanka Accounting Standards (LKAS/SLFRS) which were in effect up to that date. The Significant Accounting Policies adopted in the preparation of Financial Statements of the Company are given on pages 295 to 302 of the Annual Report as required by the Section 168 (1) (d) of the companies Act No 07 of 2007.the Board of Directors wish to confirm that there were no changes to the Accounting Policies used by the Company during the year.

2.7 Interest Register

The Interests Register is maintained by the Company, as per the Section 168(1) (e) of the Companies Act No 7 of 2007.All Directors have made declarations as provided for in section 192(1) & (2) of the Companies Act aforesaid. The related entries were made in the Interest Register during the year under review. The share ownership of Directors is disclosed on page 274 of this report, Entries were made in the Interests Register on share transaction, Directors' interest in contracts, and remuneration paid to the Directors etc. The Interest Register is available for inspection by shareholders or their authorised representatives as required by section 119 (1) (d) of the Companies Act No 07 of 2007.

2.8 Corporate Donations

During the year company made donations amounting to Rs. 1.031mn (2016-Rs. 6.064 mn).The donations made to the Government approved charities from the above amounted is Rs Nil (2016 –Nil).The information given above on donations forms integral part of the Report of the Board of Directors as required by section 168(1) (g) of the companies Act No 07 of 2007.

The details of profit relating to the Company are tabled below.

As at March 31	2017	2016
Profit before Tax	313,679	802,645
Taxation	111,665	297,626
Profit after Tax	202,014	505,019
Other Comprehensive Income	(4,011)	(10,435)
Balance brought forward	1,123,726	900,184
Available for Appropriation	1,321,729	1,394,768
Transfer to Statutory Reserve	(30,000)	(50,000)
Transfer to General Reserve	-	(200,000)
Transfer to Investment Fund	-	-
Interim Dividend Paid	-	(21,042)
Balance carried forward	1,291,729	1,123,726

2.9 Future Developments

Future developments activities of the Company are discussed under the Managing Director's report on page 22 t0 28 of this Annual Report.

3 Gross Income

The income of the Company for the year ended March 31, 2017 was Rs. 5,645 Million (year ended March 31, 2016- Rs. 4,500 Million). An analysis of income is given in Notes 6 & 7 to the Financial Statements on page 303 of this Annual Report

4 Dividend and Reserves

4.1 Profit and Appropriations

The profit before income tax of the Company for the year ended 2017 was Rs. 313 Million (Rs. 803 Million in 2016) and the profit after tax for the year ended 2017 was Rs 202 Million (Rs 505 Million in 2016)

4.2 Dividend on Ordinary Shares

Dividend not declared for this financial year.

4.3 Provision for Taxation

Income tax for 2017 has been provided at 28% (28% - 2016) on the taxable income arising from the operations of the Company and has been disclosed in accordance with Sri Lanka Accounting Standards. Profits of the Company are also liable for Value Added Tax on Financial Services at the rate of 15% (11% -2016), Crop Insurance Levy of 01% Which was introduced from January 2014.

The Company has also provided deferred tax on all known temporary differences under the liability method, as permitted by the Sri Lanka Accounting Standard - LKAS 12 on "Income Taxes"

Information on Income Tax Expenses & Differed Taxes is given in Notes 15 & 37 to the Financial Statements on pages 309 & 337 respectively, of this Annual Report.

4.4 Reserves

A summary of reserves of the Company as at year ended 31st March 2017 is as follows

	2017	2016
Statutory Reserve Fund	661,400	631,400
Revaluation Reserve	1,084,974	1,084,346
Associate Company Reserve	450,087	455,270
General Reserve	4,086,430	4,086,430
Available for sale Reserve	256,644	237,060
Retain Earnings	1,291,730	1,123,728

The Company's total Reserves as at March 31, 2017 amounted to Rs. 7,867 Million (2016–Rs. 7,654 Million). The movement of the reserves are given on page 292 under Statement of Changes in Equity & Note 39 to 44 to the Financial Statements of this Annual Report.

5. Property, Plant & Equipment & Leasehold Property & Intangible Assets

Capital expenditure incurred on Property Plant & Equipment, Intangible assets,Leasehold Property are as follows.

	2017 Million	2016 Million
Property, Plant & Equipment	85	106
Leasehold Property	Nill	Nill
Intangible Assets	2.9	3.5

Details of which are given in Note 31 to 33 on page 327 to 324 in the Financial Statements. Capital expenditure approved and contracted for is given in Note 45 to the Financial Statements on page 341 of this Annual Report.

6. Market Value of Freehold Properties

All freehold land and buildings of the Company were revalued by a professionally qualified independent valuer as at March 31, 2015, and brought into the Financial Statements. The Directors' are of the opinion that the revalued amounts are not in excess of the current market values of such properties. The details of freehold properties owned by the Company are given in Notes 31.3 to the Financial Statements on page 330.

7 Stated Capital and Debentures

The stated capital of the Company as at March 31, 2017 was Rs. 36 Million comprising 3,006,000 ordinary shares.(2016- Rs.36 Million).The details of the stated capital are given in Note 39 to the Financial Statements on page 339 of this Annual Report.

The Company had issued 2,000,000 unsecured,subordinated ,redeemable debentures of Rs.100/- each to the value of Rs 200 mn as at year ended March 31,2017.

The Company did not issue any debenture during the financial year ended March 31, 2017.

8 Share Information

8.1 Information on Earning, Dividend, Net Assets and Market Value

Information relating to earnings, dividends, net assets per share and market value per share is given in the Financial Highlights on page to Information on the trading of the shares and movement in the number of shares represented by the Stated Capital of the Company is given in the section on 'Investor Relation on pages 112 to 113.

8.2 Distribution Schedule of Shareholdings

Information on the distribution of shareholding and the respective percentages are given in the Section on 'Investor Relation'on pages 112 to 113.

8.3 Issue of shares

The Company did not make any share issues during the year under review.

Class of Shares	Voting Ordinary shares	
	2017	2016
Number of share issued	Nil	Nil

9 Substantial Shareholdings

The list of 20 Largest Shareholders as at 31 March 2017 are as follows.

Nilaveli Beach Hotel (Pvt) Ltd	629,580
Mr. G.G Ondaatjie(MD)	477,213
Ms. A.M Ondaatjie	477,213
Mr. T.J Ondaatjie	477,213
Mercantile Fortunes (Pvt) Ltd	414,160
Mr. G.L.A.Ondaatjie	268,535
Tangerine Tours (Pvt) Ltd	203,809
Mrs. P.R. Divitotawela /R.D.Madugalla	12,525
Mrs. P.R. Divitotawela /A.D.Galagoda	12,525
Mr. N.H.V.Perera	10,020
Mr.R.M.D.Abeygunewardena	10,020
Mr. J.A.S.S.Adhihetty	10,020
Mrs. C.A.Ondaatjie	2,004
Mr. A.D.Rajapaksha	501
Mr. A.M.Rajapaksha	501
Mr.A.M.Dominic & J S Dominic	151
Mr.H.W.M.Woodward	10

Names of the top twenty shareholders shares, percentages of their respective holdings and percentage holdings of the public ,etc are given in the Section on 'Investor Relations' on page 113.

9.1 Equitable Treatment to all Stakeholders

While valuing the patronage of all our stakeholders, the Company has made all endeavours to ensure equitable treatment to all our shareholders

10 Board of Directors

10.1 Information on Directors of the Company

10.1.1 List of Directors

The Board of Directors of the Company as at March 31 2017 comprised of Ten Directors (Ten Directors as at March 31, 2016) with extensive financial & commercial knowledge and experience. The qualifications and experience of the Directors are given in the 'Board of Directors – Profile' on pages 174 and 177 of this Annual Report.

Names of the persons holding office as Directors of the Company as at the end of the year and the names of persons , who ceased to hold office as Directors of the Company any time during the year 2017,as required by section 168(1) (h) of the companies Act No 07 of 2007 are given below.

Annual Report of the Board of Directors

Name of the Director	Executive/Non Executive	Independence/Non Independency
Mr. S.H.J.Weerasuriya	Non Exective	Independent
Mr. G.G.Ondaatjie	Exective	Non Independent
Mr. P.M.Amarasekara	Exective	Non Independent
Ms. A.M.Ondaatjie	Exective	Non Independent
Mr. T.J.Ondaatjie	Exective	Non Independent
Mr. S.H.Jayasuriya	Exective	Non Independent
Ms. P.T.K.Navaratne	Non Exective	Independent
Mr. N.H.V.Perera	Non Exective	Non Independent
Mr. S.M.S.S.Bandara	Non Exective	Independent
Mr. P C Guhashanka	Non Exective	Independent

10.1.2 New Appointments & Resignations

The information on new appointments and registration to and from the Board of Directors of the Company are given below.

New Appointments

There were no new appointments during the financial year.

Resignation/Cessations

There were no resignations/cessations during the financial year.

10.1.3 Recommendation for Re-election

In terms of Article 23(7) of the articles of association,Mr P M Amarasekara, Ms A M Ondaatjie and Mr.T.J.Ondaatjie retire by rotation and being eligible offer themselves for re-election.

10.1.4 Directors' Meetings

Details of the meetings of the Board of Directors are presented on page 198.

10.1.5 Board Sub-Committees

Information with regard to Board subcommittees is given under Corporate Governance on pages 190 to 193 of this Annual Report.

Board Audit Committee

All members of the Audit committee are Non-Executive Directors. The MD/CEO, Senior Management Committee members, Internal and External auditors attend the meetings by invitation. The Board Audit Committee report is given on page 284 of this Annual Report.

Integrated Risk Management Committee

The Board of Directors has established a comprehensive risk management system in the Company to identify, evaluate and manage the risks associated with the operations of the Company. A detailed overview of the process is set out in the Integrated Risk Management Committee Report on the page 281 of this Annual Report.

Nomination Committee

The Report of the Nomination Committee is given on page 283 of this Annual Report.

Remuneration Committee

The Report of the Remuneration Committee is given on page 282 of this Annual Report.

Related Party Transaction Review Committee

The report of the Related Party Transaction Review Committee is given on page 285 of this Annual Report.

10.1.6 Directors' Remuneration & Other Benefits

Directors' remuneration & other benefits , in respect of the Company for the financial year ended March 31, 2017 is given in Note 13.1 to the Financial Statements on page no 308 of this Annual Report as required by section 168(1)(f) of the companies Act No 07 of 2007.

11 Disclosures of Directors Dealing in Shares

11.1 Directors' interest in ordinary shares of the Company

	2017	%	2016	%
Mr. G.G Ondaatjie	477,213	15.87	477,213	15.87
(Managing Director/CEO)				
Ms. A.M Ondaatjie	477,213	15.87	477,213	15.87
Mr. T.J Ondaatjie	477,213	15.87	477,213	15.87
Mr.S.H.Jayasuriya	Nil	Nil		
Mr.P.M.Amarasekera	Nil	Nil		
Mr.S.H.J.Weerasuriya	Nil	Nil		
Ms.P.T.K.Navaratne	Nil	Nil		
Mr.N.H.V.Perera	10,020	0.33	10,020	0.33
Mr.S.M.S.S.Bandara	Nil	Nil		
Mr.P C Guhashanka	Nil	Nil		

11.1.1. Mr. G.G. Ondaatjie serves as the Managing Director as well as Chief Executive Officer to the Company.

11.1.2 The number of ordinary shares held by the public as at March 31, 2017 was 316,792 shares (2016- 326,812) which amounted to 10.54% (2016- 10.87%) of the stated capital of the Company.

11.1.3 Directors Interest in Debentures

There were no debentures registered in the name of any Director as at the beginning and at the end of the year.

12 Directors Interests in Contracts or Proposed Contracts and Related Party Transaction.

Directors have no direct or indirect interest in any contract or proposed contract with the Company for the year ended March 31, 2017. Further information is given on page 277 to 278 of this Annual Report. The Directors have also disclosed transactions if any that could be classified as Related Party Transactions in terms of the Sri Lanka Accounting Standard – LKAS 24 on 'Related Party Disclosures'. Please refer note 48 to the Financial Statements on pages 341 to 343 for those transactions disclosed by the Directors. These interests have been declared at Related Party Transaction Review Committee Meetings.

There are no related party transactions which exceed 10 percent of the total Equity or 5 percent of the total assets whichever is lower and the Company has complied with the requirements of the listing rules of the Colombo Stock Exchange on Related Party Transactions.

The Directors have disclosed their interest in other companies so as to ensure that they refrain from voting on a matter in which they have an interest.

13 Employee Share Option Plans and Profit Sharing Plans

The Company do not have any employee profit sharing plan or employee share option plans.

14 Environmental Protection

The Directors, to the best of their knowledge and belief, are satisfied that the Company has not engaged in any activities, which have caused adverse effects on the environment and it has complied with the relevant environmental regulations.

15 Statutory Payments

The Directors, to the best of their knowledge and belief, are satisfied that all statutory payments in relation to the Government and employees have been paid up to date.

16 Events after the Balance Sheet Date

There have been no material events occurring after the balance sheet date that would require adjustments to or disclosure in the financial statements as disclosed in Note 50 to the Financial Statements on page 344 of this Annual Report.

17 Going Concern

The Board of Directors had reviewed the Company's business plans and is satisfied that the Company has adequate resources to continue its operation in the foreseeable future. Accordingly, the Financial Statements of the Company prepared based on the going concern concept.

18 Appointment of External Auditors

According to the guideline issued by the monetary board of the Central Bank of Sri Lanka under Sec 30(2) of the Finance Business Act, No 42 of 2011, Company required to appoint an external auditor from the panel of external auditors listed in the said guideline. Therefore Messrs BDO partners were appointed as auditors of the Company and the financial statements for the year ended 31st March 2017 have been audited by them.

A resolution proposing Messers. Ernst & Young, Chartered Accountants to be appointed as Auditors of the company for the year 2017/18 and authorising directors to determine their remuneration will be submitted at the Annual General Meeting.

19 Auditors' Remuneration and Interest in Contracts with the Company

The Auditors, Messrs BDO Partners were paid Rs 1.5 Million (Rs 1.4 Million in 2016 to Messrs BDO Partners) as audit fees by the Company. Apart from that the Company has not engaged external auditors for any other permitted non-audit services.

As far as the Directors are aware, the auditors do not have any other relationship or interest in contracts with the Company.

20 Risk Management & System of Internal Controls

20.1 Risk Management

Specific steps that have been taken by the Company in place to identify, evaluate and manage both business risk & financial risk are detailed on pages 349 to 360 of this Annual Report

20.2 System of Internal Controls

The Board of Directors has established an effective and comprehensive system of Internal Controls to ensure that proper controls are in place to safeguard the assets of the Company, to detect & prevent fraud & irregularities, to ensure that proper records are maintained and Financial Statements presented are reliable. Monthly Management Accounts are prepared, giving management with relevant, reliable and up to date Financial Statements and key performance indicators.

The Audit Committee reviews on regular basis, the reports, policies and procedures to ensure a comprehensive Internal Control framework is in place. More details in this regard can be seen in the 'Audit Committee Report' on page 284 of this Annual Report.

20.3 Audit Committee

The composition of the Audit Committee and their report is given on page 284 of this Annual report.

21 Corporate Governance

Directors Declarations

The Directors' Declare that –

- » The Company has not engaged in any activity which contravenes laws and regulations.
- » The Company has made all endeavours to ensure the equitable treatment of shareholders.
- » The business is going concern.
- » Effectiveness and successful adherence of internal controls and risk management is practiced by the Company.
- » The measures taken in this regard are set out in the corporate governance report on pages 182 to 242 this annual report.
- » To the best of their knowledge there has not been any violation of the code of business conduct and ethics of the Company.

The measures taken and the extent to which the Company has complied with the Code of best Practice on Corporate Governance issued by The Institute of Chartered Accountants of Sri Lanka and Securities and Exchange Commission of Sri Lanka, the CSE and the Central Bank of Sri Lanka are given in the section on 'corporate governce' on pages 182 to 242.

22 Human Resources

The Company continues to regard communication with its employees as a key aspect of its policies. Information is given to employees about employment matters and about the financial and economic factors affecting the Company's performance. Employees are encouraged to discuss operational and strategic issues with their line management and to make suggestions aimed at

Annual Report of the Board of Directors

improving performance. Specific measures taken in this regard are detailed in the Human Capital Report on pages 116 to 127 of this Annual Report. Further The Board made a declaration in this year's Director's Report stating "All the members of Board of Directors and key management personnel have complied with code of business conduct and ethics introduced in the HR Handbook".

23 Compliance with Applicable Laws and Regulations

To the best of our knowledge there has been no violation or possible violation of laws or regulations in any jurisdiction other than the matter discussed in Note 22.3 to the Financial Statement on Page 318 and Note 53 to the Financial Statement on Page no 354. There have been no irregularities involving management or employees that could have material financial effect or otherwise.

24 Outstanding Litigation

In the opinion of the Directors and in consultation with the Company Lawyers, litigation currently pending against the Company will not have material impact on the reported financial results or future operations of the Company.

25 Notice of Meeting

The details of the Annual General Meeting are given in the notice of meeting on page 372 of this Annual Report.

26 Acknowledgement of the contents of the Report

As required by section 168(1)(k) of the Companies Act No 07 of 2007 the Board of Directors hereby acknowledge the contents of this report.

G.G. Ondaatjie
Managing Director

A.M. Ondaatjie
Director

Ms. Sonali Pethiyagoda
Company Secretary

Colombo
14 September 2017

Directors' Interests in Contracts with the Company

Outstanding balances of accommodation granted/ deposit received/ receivable in respect of services rendered as at the reporting date with the entities where the chairman or a director of the Company is the chairman or director of such entities.

Company	Relationship	Accommodation granted / deposits / receivable for services rendered / payable for services obtained	As at 31.03.2017 Rs.'000	As at 31.03.2016 Rs.'000
a) Mr. G. G. Ondaatjie				
Mercantile Fortunes (Pvt) Limited	Managing Director	Motor vehicle hire, repairs and others	1,522	10
Tangerine Beach Hotels PLC	Director	Deposits	227,551	114,802
		Loan	5,377	9,678
		Motor vehicle hire, repairs and others	(111)	79
Royal Palms Beach Hotels PLC	Director	Deposits	165,144	161,407
		Loan	2,378	4,653
		Motor vehicle hire, repairs and others	185	109
Nuwara Eliya Hotels Company PLC	Managing Director	Deposits	590,264	456,794
		Motor vehicle hire, repairs and others	4	3
Tangerine Tours (Pvt) Limited	Director	Deposits	114,480	105,128
		Motor vehicle hire, repairs and others	283	125
Nilaweli Beach Hotels (Pvt) Limited	Ex. Deputy Chairman	Deposits	135,351	161,039
		Motor vehicle hire, repairs and others	44	-
Security Ceylon (Pvt) Limited	Director	Deposits	3,158	3,072
		Motor vehicle hire, repairs and others	(4)	-
		Security expenses	2,572	2,703
Mercantile Orient (Pvt) Limited	Managing Director	Deposits	5,249	4,894
Global Films Limited	Director	Deposits	1,264	1,169
Fair View Hotel (Pvt) Limited	Chairman/ Managing Director	Deposits	42,898	14,000
b) Ms. A.M. Ondaatjie				
Mercantile Fortunes (Pvt) Limited	Director	Motor vehicle hire, repairs and others	1,522	10
Tangerine Beach Hotels PLC	Joint Managing Director	Deposits	227,551	114,802
		Loan	5,377	9,678
		Motor vehicle hire, repairs and others	(111)	79
Royal Palms Beach Hotels PLC	Joint Managing Director	Deposits	165,144	161,407
		Loan	2,378	4,653
		Motor vehicle hire, repairs and others	185	109
Nuwara Eliya Hotels Company PLC	Director	Deposits	590,264	456,794
		Motor vehicle hire, repairs and others	4	3
Tangerine Tours (Pvt) Limited	Joint Managing Director	Deposits	114,480	105,128
		Motor vehicle hire, repairs and others	283	125
Nilaweli Beach Hotels (Pvt) Limited	Director	Deposits	135,351	161,039
		Motor vehicle hire, repairs and others	44	-
Security Ceylon (Pvt) Limited	Director	Deposits	3,158	3,072
		Motor vehicle hire, repairs and others	(4)	-
		Security expenses	2,572	2,703
Mercantile Orient (Pvt) Limited	Director	Deposits	5,249	4,894
Global Films Limited	Director	Deposits	1,264	1,169
Fair View Hotel (Pvt) Limited	Director	Deposits	42,898	14,000

Directors' Interests in Contracts with the Company

Company	Relationship	Accommodation granted / deposits / receivable for services rendered / payable for services obtained	As at 31.03.2017 Rs.'000	As at 31.03.2016 Rs.'000
c) Mr. T.J. Ondaatjie				
Mercantile Fortunes (Pvt) Limited	Director	Motor vehicle hire, repairs and others	1,522	10
Tangerine Beach Hotels PLC	Director	Deposits	227,551	114,802
		Loan	5,377	9,678
		Motor vehicle hire, repairs and others	(111)	79
Royal Palms Beach Hotels PLC	Director	Deposits	165,144	161,407
		Loan	2,378	4,653
		Motor vehicle hire, repairs and others	185	109
Nuwara Eliya Hotels Company PLC	Director	Deposits	590,264	456,794
		Motor vehicle hire, repairs and others	4	3
Tangerine Tours (Pvt) Limited	Director	Deposits	114,480	105,128
		Motor vehicle hire, repairs and others	283	125
Nilaweli Beach Hotels (Pvt) Limited	Managing Director	Deposits	135,531	161,039
		Motor vehicle hire, repairs and others	44	-
Security Ceylon (Pvt) Limited	Director	Deposits	3,158	3,072
		Security expenses	2,572	2,703
		Motor vehicle hire, repairs and others	(4)	-
Mercantile Orient (Pvt) Limited	Director	Deposits	5,249	4,894
Global Films Limited	Director	Deposits	1,264	1,169
Fair View Hotel (Pvt) Limited	Director	Deposits	42,898	14,000
d) Mr. S.H. Jayasuriya				
Mercantile Fortunes (Pvt) Limited	Director	Motor vehicle hire, repairs and others	1,522	10
Security Ceylon (Pvt) Limited	Director	Deposits	3,158	3,072
		Security expenses	2,572	2,703
		Motor vehicle hire, repairs and others	(4)	-
e) Mr. P.M. Amarasekara				
Security Ceylon (Pvt) Limited	Director	Deposits	3,158	3,072
		Security expenses	2,572	2,703
		Motor vehicle hire, repairs and others	(4)	-
Fair View Hotel (Pvt) Limited	Director	Deposits	42,898	14,000
f) Mr. N.H.V. Perera				
Tangerine Beach Hotels PLC	Director	Deposits	227,551	114,802
		Loan	5,377	9,678
		Motor vehicle hire, repairs and others	(111)	79
Royal Palms Beach Hotels PLC	Director	Deposits	165,144	161,407
		Loan	2,378	4,653
		Motor vehicle hire, repairs and others	185	109

Directors’ Responsibility for Financial Reporting

The following statement sets out the responsibilities of the Directors in relation to the preparation and presentation of the Financial Statements of the Company.

As per Section 148 (1) and 151 (1) of the Companies Act No. 07 of 2007, Directors of the Company have the responsibility for ensuring that the Company keeps proper books of account of all the transactions and prepare Financial Statements that give a true and fair view of the state of affairs and of the profits / losses for the year.

Accordingly, the Directors have caused the Company to maintain proper books of account and reviewed the financial reporting system at their regular meetings and through the Audit Committee. The Audit Committee Report is given on page 284 of this Annual Report. The Financial Statements consist of the Statement of Financial Position as at 31st March 2017, and the Statement of Comprehensive Income, Statement of Changes in Equity and Statement of Cash Flows for the year then ended and notes thereto, prepared and presented in this Annual Report are consistent with the underlying books of account and are in conformity with the requirements of the Companies Act, Sri Lanka Accounting Standards, the Finance Business Act No 42 of 2011.

Further the Directors have a responsibility to ensure that the Company maintains sufficient accounting records to disclose, with reasonable accuracy, the financial position of the Company. The Directors consider that, in preparing the Financial Statements exhibited from pages 290 to 294 inclusive, they have adopted appropriate accounting policies and standards on a consistent basis and supported by reasonable and prudent judgments and estimates.

The Directors ensure that the Company has adequate resources to continue in operation to justify applying the going concern basis in preparing these Financial Statements.

The Directors also have the responsibility to ensure that the Company maintains adequate general supervision, control and administration of the affairs and business of the Company.

The Directors are of the opinion that the Internal Control System, in place, is capable of safeguarding the assets, preventing and detecting fraud and errors, ensures accuracy and completeness of the accounting records and timely preparation of reliable financial information.

The Board of Directors accepts responsibility for the integrity and objectivity of the Financial Statements presented in this Annual Report.

The Directors confirm that to the best of their knowledge all taxes, statutory dues and levies payable by the Company as at the reporting date have been paid or where relevant, provided for. The Directors also confirm that all shareholders have been treated in an equitable manner.

The Company’s Auditors, Messrs BDO Partners, carry out reviews and sample checks on the system of internal controls as they consider appropriate and necessary for expressing their opinion on the Financial Statements.

Messrs BDO Partners, the Auditors of the Company have examined the Financial Statements made available by the Board of Directors together with all the financial records, related data and minutes of Shareholders and Directors’ meetings and express their opinion which appears as reported by them on page 288 of this Annual Report.

Accordingly, the Directors are of the view that they have discharged their responsibilities as set out in this statement.

By order of the Board,

Mercantile Investments and Finance PLC
Ms. Sonali Pethiyagoda
Company Secretary

12 September 2017

Managing Director's and Chief Financial Officer's Statement of Responsibility

The Financial Statements of Mercantile Investments and Finance PLC are prepared and presented in accordance with the following requirements:

» Sri Lankan Financial Reporting Standards (SLFRS/LKAS) issued by The Institute of Chartered Accountants of Sri Lanka;

» The Companies Act No. 07 of 2007;

» Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995;

» Directions issued to Finance Companies by the Central Bank of Sri Lanka (CBSL) under the Finance Business Act No. 42 of 2011;

» Listing Rules of the Colombo Stock Exchange; and

» The Code of Best Practice on Corporate Governance issued jointly by The Institute of Chartered Accountants of Sri Lanka and the Securities and Exchange Commission of Sri Lanka.

The Accounting Policies adopted in the preparation of the Financial Statements are appropriate and have been consistently applied during the financial year under review. 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 and material departures, if any, have been disclosed and explained. Significant accounting policies and estimates that involved a high degree of judgement and complexity were discussed with External Auditors and the Board Audit Committee.

The Board of Directors and the Management of the Company accept responsibility for the integrity and objectivity of these Financial Statements to the best of our knowledge.

Material estimates and judgement relating to the Financial Statements were made on a prudent and reasonable basis, in order to ensure that the Financial Statements are reflected in a true and fair manner. The form and substance of transactions reasonably represent MI's state of affairs. To ensure this, the Company has taken 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 Internal Auditors have conducted periodic audits to provide reasonable assurance that the established policies and procedures of the Company 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. Further, the Board assessed the effectiveness of the Company's internal controls over financial reporting during the year ended 31st March 2017, as required by the Finance Companies (Corporate Governance) Direction No. 3 of 2008, result of which is given on page 286 of this Annual Report, the 'Report by the Board on Internal Control'.

The Audit Committee meets periodically with the Internal and External Auditors to review the manner in which the auditors carry out their responsibilities in performing their duties and to discuss audit findings, and any deficiencies in internal controls that may impact the accuracy and completeness of the financial reporting process.

The Financial Statements of the Company were audited by Messrs BDO Partners and their Audit Report is given on page 288 of this Annual Report.

The Audit Committee has reviewed and recommended the scope and fees of audit and non-audit services, provided by the External Auditors for approval of the Board of Directors to ensure that the provision of such services does not impair the Auditor's independence and objectivity. Both Internal and External Auditors have full and free access to the members of the Audit Committee to discuss any matter of substance.

We confirm that the Company has complied with all applicable laws, regulations and prudential requirements, and there are no material litigations pending against MI other than those disclosed in note no. 22 and note no. 53 of the Financial Statements in this Annual Report. All taxes, duties and statutory payments by the Company and in respect of the employees of MI as at 31st March 2017 have been paid or where relevant accrued.

G.G. Ondaatjie
Managing Director

Shermal Jayasuriya
Finance Director/Chief Financial Officer

12 September 2017

Integrated Risk Management Committee Report

The Composition of the Integrated Risk Management Committee

The Committee consists of the following members:

Name	Membership Status	Directorship Status/ Position held in the Company
Mr. N.H.V. Perera	Chairman	Non-Executive Director
Mr. Gerard G. Ondaatjie	Member	Executive Director
Mr. P.M. Amarasekara	Member	Executive Director
Mr. S.H. Jayasuriya	Member	Executive Director
Mr. Shehan Sandanayaka	Secretary	Manager – Risk & Compliance

Integrated Risk Management Committee (IRMC)

The IRMC was established by the Board of Directors, in keeping with Sections 8.1 and 8.3 of the Finance Companies (Corporate Governance) Direction No. 3 of 2008 issued by the Monetary Board under the Finance Companies Act No. 78 of 1988. The scope and functions of the Committee conforms to the provisions of Section 8.3.b of the aforesaid Direction.

The Committee held four meetings for the year under review. The attendance of each member at meetings is illustrated in the table given on page 190 of this Annual Report.

Duties and Responsibilities of the Committee

Based on the Board approved 'Terms and Reference' and 'Risk Policy' developed, following are the key responsibilities of the Integrated Risk Management Committee.

a. Assess the adequacy and effectiveness of the risk profile of Mercantile Investments and Finance PLC.

b. Establish a method of overseeing the overall risk management procedures of the Company. Set the tone and influence the culture of risk management within Mercantile Investments and Finance PLC.

   This includes:

   » Communicating MI’s approach to risk

   » Determining what types of risk are acceptable and which are not

   » Setting the standards and expectations of staff with respect to conduct and integrity.

c. Determine the appropriate Risk Appetite or tolerable exposure ranges for the purpose of assessing risk, where risk tolerance levels help to ensure appropriate reporting and monitoring processes, for the effective management of identified risks.

d. Approve major decisions affecting MI’s risk profile or exposure and ensure risk assessment decisions are taken within the framework of the authority and responsibility assigned to the Committee.

e. Identify risks and monitor the management of fundamental risks to reduce the likelihood of unwelcome surprises.

f. Satisfy that the less fundamental risks are being actively managed, with the appropriate controls in place and working effectively.

g. Periodically review MI’s approach to risk management and approve changes or improvements to key elements of its processes and procedures.

Terms of Reference

The Board Integrated Risk Management Committee is responsible for,

» Assessing all risks including, credit, liquidity, operational and strategic risks periodically, through appropriate risk indicators; and

» Depending on the level of risk prevalent, taking measures to effect corrective actions to mitigate the effects of an identified risk of very high nature or risks exceeding prudent levels considering the Company's policies and regulatory requirements.

Approach Adopted by the Integrated Risk Management Committee

1. The Committee has the right blend of members who currently represent the core divisions covering areas in credit, recoveries and finance while its Chairman appointed in 2012 is a Non-Executive Director of the Board.

2. During this financial period, the Committee activities revolved around the following broad functions:

» Communicated with the relevant Heads of Divisions on the needed course of action to improve the overall effectiveness of risk management at MI.

» Reviewed and approved risk parameters and limits against various categories of risks and assessed whether they are aligned with the relevant laws and regulations and MI’s policies.

» Submitted quarterly 'Activity Report' to the Board to update Directors on key risk related matters and to convey recommendations made by the Committee.

3. Reviewed the operation of ALCO and the Management Committee and verified following:

» ALCO was able to review and resolve mismatches in maturity profiles of assets and liabilities and lending and borrowing behaviour of the Company along with competitor strategy review.

» Management committee reviewed ongoing performance to provide early warning signs and a platform for decision-making through provision of MIS.

» Reviewed efforts of the Sustainability Governance Committee in meeting MI’s economic, social and environmental obligations and associated risk, if not handled properly.

» Reviewed compliance status of MI to prevailing laws and regulations with specific focus on CBSL requirements.

N.H.V. Perera
Chairman
Integrated Risk Management Committee

12 September 2017

Remuneration Committee Report

Committee Composition

The Committee comprises of three Non-Executive Directors and is chaired by Mr. S.H.J Weerasuriya who is an Independent Non-Executive Director of the Company.

Name	Membership Status	Directorship status/Position held in the Company
Mr. S.H.J.Weerasuriya	Chairman	Independent Non- Executive Director
Mr. N.H.V.Perera	Member	Non- Executive Director
Ms. P.T.K.Navaratne	Member	Independent Non- Executive Director
Ms. Sonali Pethiyagoda	Secretary	Company Secretary

Terms of Reference

» Recommend and approve total remuneration package and incentivisation package of the Executive Directors.

» Consider and recommend to the Board the broad policy for the remuneration and incentivisation package.

» Review company's remuneration practices and policies to ensure fairness in Directors' Remuneration.

» Determine the policy for the terms of employment of the Executive Directors.

» Monitor performance conditions subject to which any long term incentive awards may be granted under the schemes adopted by the Company and approve grant of long term incentive awards, such as share appreciation rights and performance shares.

» Review the design of all share incentive schemes.

» Bear the responsibility for selecting and appointing any remuneration consultants who advise the Committee.

Committee's Role

The Committee is responsible for setting up the remuneration policy and making recommendations to the Board on the following matters:

» Set guidelines and policies to formulate compensation packages, which attract and motivate qualified and experienced personnel to the Board of the Company.

» A competitive and fair remuneration package payable to the Executive Directors including the Managing Director of the Company, which is satisfactory to both the interests of the shareholders and the members in concern.

» Evaluating the prevailing market remuneration levels when making remuneration policy amendments.

Guiding principles when setting remuneration

» In order to remunerate individuals in an effective manner, the Board has set forth guiding principles that should be followed when deciding on remuneration.

» Deciding on standard pay that will enable the Company to attract and retain high calibre personalities.

» Remuneration should be aligned in a way that it satisfies both shareholders and members interests.

» The Committee to meet annually to recommend increments to the Managing Director and Executive Directors.

» Evaluating the prevailing remuneration levels in the market in general when deciding on salary revisions.

Meeting information

The number of Committee meetings held during 2016/17 with attendance status of members is given on page 190 in the Annual Report.

Saro Weerasuriya
Chairman
Remuneration Committee

12 September 2017

Nomination Committee Report

Composition of the Nomination Committee

The Nomination committee comprises of the following Directors of MI.

Name	Membership Status	Directorship Status/Position held in the Company
Mr. S.H.J Weerasuriya	Chairman	Independent Non – Executive Director
Mr. Gerard G.Ondaatjie	Member	Managing Director
Mr. N.H.V. Perera	Member	Non-Executive Director
Mr. S.M.S.S. Bandara	Member	Independent Non – Executive Director
Ms. Sonali Pethiyagoda	Secretary	Company Secretary

Objectives of the Committee

The Nomination Committee was established by the Mercantile Investments and Finance PLC Board of Directors in order to strengthen the Director appointment process specifically focusing on:

- » Identifying individuals qualified to serve as Board members, consistent with criteria approved by the Board;
- » Recommending to the Board, the Director nominees for election or appointment after ascertaining the necessity of additional Directors; and
- » Conducting a rigorous and transparent process when making or renewing appointments of Directors to the Board. It also advises the Board on issues of Directors' independence.

Committee Duties, Responsibilities and Process

- » Conduct continuing study of the size, structure and composition of the Board and make appointments of new Directors or re-elect current Directors to the Board.
- » Seek out possible candidates to fill Board positions, and advice and recommend to the Board on any such appointment.
- » Evaluate nominees based on criteria such as qualifications, experience and key attributes required for eligibility to be considered for appointment or promotion to the post of Director or key management submitted by any shareholder of the Company.
- » Recommend to the Board, prior to the solicitation of proxies, an account of qualified candidates for election to the Board at each meeting of shareholders of the Company at which Directors are to be elected and, in the case of a vacancy on the Board, a candidate to fill that vacancy.
- » Evaluate the performance of incumbent Directors upon the expiration of their terms.
- » Ensure balance of skill, knowledge and experience of members forming part of the Board and also ensure that the members are fit and proper persons to hold the position as required by statutes.
- » Prepare evaluation forms for all Board members and all members of Board committees and, at least annually, receive comments from all members of the Board and report to the Board with an assessment of the Board's performance.
- » Oversee the orientation and training of new Directors.
- » Recommend ways in which the Board could improve its performance.

Meeting information

The number of Committee meetings held during financial year 2016/17 with attendance status of members is given on page 190 in the Annual Report.

Saro Weerasuriya
Chairman
Nomination Committee

12 September 2017

Audit Committee Report

The Board of Directors has established the Audit Committee in accordance with Best Practices on Audit Committees. The Audit Committee comprises of two Independent Non-Executive Directors, a Non-Executive Director and a Secretary for the Committee. The Committee is chaired by an Independent Non-Executive Director while the Company Secretary functions as the Secretary to the Committee.

Name	Membership Status	Directorship Status/Position held in the Company
Mr. S M S S Bandara	Chairman	Independent Non-Executive Director
Mr. S H J Weerasuriya	Member	Independent Non-Executive Director
Mr. N H V Perera	Member	Non-Executive Director
Ms. Sonali Pethiyagoda	Secretary	Company Secretary

Terms of Reference

The Terms of Reference of the Audit Committee stems from the scope of the Board Audit Committee. Terms of References are established for the purpose of assisting the Board in fulfilling their responsibilities, including risk management, integrity of financial statements, internal control, compliance etc.

During the period, the Finance Director and representatives from Internal Auditors and External Auditors were present at meetings by invitation.

The Board of Directors have empowered among other things, to examine any matter in connection with financial and other related affairs of the Company, to review internal audit programmes, internal control system and procedures, accounting policies and the compliance with statutory and regulatory requirements etc., thus ensuring that a sound financial reporting framework is in place, which is well-monitored to provide accurate, appropriate and timely information to the Board of Directors, Management, Regulatory Authorities and Shareholders.

The Audit Committee assures that the Company's policies and activities comply with rules and regulations and accepted ethical guidelines. Establishing effective risk management processes that enable the proper identification and mitigation of risk is one of the key objectives of the Audit Committee. Assisting the Board of Directors in fulfilling its oversight responsibilities in the financial reporting process and auditing financial statements by monitoring the integrity and reliability of the financial statements is another key function of the Audit Committee.

The Committee held six meetings during the financial year 2016/17 and performed the under mentioned tasks:

1. Reviewed Internal Audit Reports on Head Office and branch activities and discussed measures to be taken on deficiencies and shortcomings that have been pointed out.
2. Regularly monitored the effectiveness of the internal controls and the procedures established by the management to safeguard the assets of the Company.
3. Met with the External Auditors at the conclusion of annual audit and reviewed the Auditors' Management Letter together with the management's response thereto.
4. Ensured the integrity of financial reporting and compliance with financial reporting requirements and other related regulations.
5. Reviewed the financial statements in order to ensure consistency of the accounting policies, methods and compliance with Sri Lanka Accounting Standards. The Annual Financial Statements were also reviewed with the External Auditors.
6. Reviewed periodically the Company's compliance with regulatory requirements and other statutory requirements.
7. Ensured that sound corporate governance practices exist within the Company.

The Audit Committee submits their report to the Board of Directors on a regular basis. The effectiveness of the Committee is evaluated by the Board of Directors at the end of each financial year.

Internal Audit

The Committee ensures that the Internal Audit Division of MI is independent of the operational activities of the Company and internal audit performs its activities impartially, diligently and professionally.

The internal audit programme is structured to ensure there is adequate audit cover both at Head Office and branch level. The Audit Committee regularly reviewed audit reports and followed-up with management on material audit observation with recommendations.

Independence of External Auditors

The Audit Committee reviews audit and non-audit functions of External Auditors which are segregated as those require independent view and other advisory services. Messrs. BDO partners external Auditors does not handle substantial volume of non-audit services of the Company in keeping to terms of reference of engagement of external audit partners to provide non-audit services.

The Audit Committee ensures that the provision of such services does not impair independence and objectivity of External Auditors and that work is assigned in such manner as to prevent any conflict of interest.

The Committee is of the view that adequate controls and procedures are in place to provide reasonable assurance that the Company's assets are safeguarded and that the financial position of the Company is well monitored.

The Audit Committee has recommended to the Board of Directors that Messrs. Ernst & Young, be appointed as the External Auditor of the Company for the year 2017/18, subject to the approval of shareholders at the Annual General Meeting, in accordance with CBSL Regulations on selecting regulatory approved External Auditors for the sector. The Audit Committee's selection and review of External Auditors was based on capability, resource availability of the firm and their level of independence from MI and Board of Directors. The Audit Committee recommended the fees payable to the Auditors in 2016/17 financial year and approved by the Board.

S. Bandara

S.M.S.S. Bandara
Chairman
Audit Committee
14 September 2017

Board Related Party Transactions Review Committee Report

Composition of the Committee

The Company established the Board-Related Party Transactions Review Committee (BRPTRC) during the financial year 2014/15. BRPTRC comprises of the following;

Name	Membership Status	Directorship Status/Position held in the Company
Mr. S.M.S.S Bandara	Chairman	Independent Non-Executive Director
Mr. S.H.J. Weerasuriya	Member	Independent Non-Executive Director
Mr. S. H. Jayasuriya	Member	Executive Director
Mr. N.H.V. Perera	Member	Non-Executive Director
Ms. Sonali Pethiyagoda	Secretary	Company Secretary

Objective

Ensure interest of MI shareholders are protected as a whole when entering into related party transactions, to have a mechanism to comply with requirements of the Code of Best Practice on Related Party issued by the Securities and Exchange Committee of Sri Lanka. Specify a process to capture related party transactions and to report to the Board as per the code of best practice.

Scope of the Committee

Identify all related parties of the Company and review all related party transactions to ensure that they are carried out on an arm's length basis. At each subsequent scheduled meeting of the Committee, the management shall update the Committee as to changes in any previously identified related parties.

Mandate of the Committee

- Developing terms of reference of the BRPTRC for adoption by the Board of Directors of the Company.
- Adopting policies and procedures to identify related parties and review of related party transactions of the Company and reviewing and overseeing existing policies and procedures.
- Establishing guidelines to be followed by the Senior Management in respect of ongoing related party transactions.
- Updating the Board of Directors on the related party transactions of the Company on a quarterly basis.
- Making immediate market disclosures on applicable related party transactions as required by Colombo Stock Exchange (CSE).
- Making appropriate disclosure on related party transactions in the Annual Report as required by CSE.
- Determining whether Related Party Transactions require the approval of the Board of Directors.
- Draw the attention of the Board on concerning transactions, if any.

Committee Meetings and Duties

- Four Committee meetings were held during the year under review. The Finance Division submitted comprehensive reports on related party transactions to the Committee. Attendance of the members of the Committee is provided on page 190. Any concerns of the Committee will be reported to the Board of Directors on a continuous basis.
- Terms of reference of the Committee was submitted to the Board for approval on 28th March 2016.
- The committee reviewed and monitored related party transactions that the Company has entered into.
- Formulated, revised and approved policies on related party transactions.
- Advised management on the reporting format to committee.

S. Bandara

S. M. S. S. Bandara
Chairman
Related Party Transactions Review Committee

12 September 2017

Report by the Board on Internal Control

Board's Responsibility

This Report on internal control has been presented in accordance with Section 10.2 (b) of the Finance Companies (Corporate Governance) Direction, No. 03 of 2008 and Corporate Governance – Amendment Direction No. 06 of 2013.

The Board of Directors is responsible for the adequacy and effectiveness of the Company's system of internal controls. The system of internal control has been however, designed to manage the Company's key risk areas within an acceptable risk profile, rather than to eliminate the risk of failure to achieve Company's policies and objectives. Hence, MI's internal control system can only provide reasonable but not absolute assurance against material misstatements of management and financial information and records or against financial losses.

The Board has established a mechanism for identifying, evaluating and managing material risks. This process includes enhancing the system of internal controls when needed in-line with changes in the business environment or regulation. The management of MI assists the Board in the implementation of the policies and procedures on risk and control by identifying and assessing the risks faced, and in the design, operation and monitoring of suitable internal controls to control risks.

Broad Process Adopted in Applying and Reviewing the design and Effectiveness of the Internal Control Mechanism on Financial Reporting

The salient processes that have been established in reviewing the adequacy and integrity of the system of internal controls pertaining to financial reporting are as follows:

- Relevant Heads of Divisions have been delegated the task of applying controls to capture their related transactions on to a defined and structured recording information system that supports in financial reporting. At the same time, the Finance Department headed by the Finance Director has been delegated the task of preparing the accounts and Annual Financial Statements in line with Sri Lanka Accounting Standards and other applicable regulations.
- MI's own Internal Audit Division and Ernst and Young Advisory Services (Pvt) Limited have been jointly entrusted with the task of carrying out the Company's internal audit function on a periodic basis to verify the compliance with policies and procedures and the effectiveness of the internal control systems and providing feedback of such reviews to the Audit Committee on any non-compliance.
- The Audit Committee of the Company meets to review internal control issues identified by Internal Auditors in their periodic reviews, External Auditors' queries raised from their statutory reviews and other matters that are important to financial reporting. The Committee evaluates the adequacy and effectiveness of Company's risk management process and internal control systems. The Committee further reviews work of Internal Auditors on their scope and quality of audits. The Committee follows up with relevant management and in turn provides feedback to the Board on any concerning matters for their deliberation and resolution.
- Other Sub-Committees appointed by the Board assist the Board in reviewing and providing feedback to the Board on the effectiveness of areas specifically entrusted upon to such Committees through periodic supervision. This includes reviewing related operations to ensure they are in line with corporate objectives, policies and established procedures.
- To strengthen reporting, additional ICT controls were established and MIS reports generated during FY 2016/17.
- Manager – Risk and Compliance submitted compliance status reports covering all applicable CBSL Rules and Regulations to the Board on a monthly basis. A branch compliance checklist, covering all the regulation and internal controls is signed off by branch managers on a bi-monthly basis to ensure higher level of compliance within MI branch network.

Confirmation by the Board

The Board is of the view that the system of internal controls in place is sound and adequate to provide reasonable assurance regarding the reliability of financial reporting. Based on the established internal control mechanism explained above, the Board confirms that the financial reporting system of the Company has been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of Financial Statements for external purposes is done in line with Sri Lanka Accounting Standards and requirements of the regulator.

External Auditors Review of the Statement

The External Auditors have reviewed the above 'Report by the Board on Internal Control' for the year ended 31st March 2017 included in the Annual Report of the Company. They reported to the Board that nothing has come to their attention that causes them to believe that the statement is inconsistent with their understanding of the process adopted by the Board in the review of the design and effectiveness of the Internal Control System of the Company over financial reporting.

By order of the Board,

S.Bandara

S.M.S.S. Bandara
Chairman
Audit Committee

Saro Weerasuriya
Chairman

G.G. Ondaatjie
Managing Director

12 September 2017

Independent Assurance Report on the Directors' Statement on Internal Control

BDO

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To the Board of Directors of Mercantile Investments and Finance PLC

Introduction

We were engaged by the Board of Directors of Mercantile Investments and Finance PLC ("The Company") to provide assurance on the Directors' Statement on Internal Control ("the Statement") included in the annual report for the year ended 31st March, 2017.

Management's responsibility

Management is responsible for the preparation and presentation of the Statement as required by section 10 (2) (b) of Finance Companies (Corporate Governance) Direction, No.3 of 2008 and Corporate Governance – Amendment Direction, No.06 of 2013. In the absence of specific detail guidelines with respect of preparation and presentation of the Statement for finance companies, in preparing and presenting the statement, the company has considered "Guidance for Directors of Banks on the Directors' Statement on Internal Control" issued in compliance with section 3 (8) (ii) (b) of the Banking Act Direction No. 11 of 2007, by the Institute of Chartered Accountants of Sri Lanka.

Our responsibilities and compliance with SLSAE 3050

Our responsibility is to issue a report to the Board on the Statement based on the work performed. In the absence of specific detail guidelines with respect of providing assurance report for finance companies on the Director's Statement on Internal Control, 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 Company.

To achieve this objective appropriate evidence has been obtained by performing the following procedures.

1. We had an initial meeting with the Senior Manager Finance and other relevant key management of the company and discussed the company's approach in assessing, designing and effectiveness of the company's internal controls over financial reporting.
2. Requested all correspondence related to Directors' Assessment on design and effectiveness of the Internal Control of the company and performed further procedures including the followings:

2.1 We independently reviewed the documentation of internal controls related to the key processes provided by the management and confirmed the completeness of such documentation by performing walkthroughs and test of controls.

2.2 We reviewed the findings by Internal Auditors related to internal control weaknesses including suggestions for improvements.

2.3 Reviewed the minutes of the meetings of the Board of Directors and of relevant Board Committees such as the Audit Committee.

3. Considered whether the Director's Statement on Internal Control covers the year under review and that adequate processes are in place to identify any significant matters arising.
4. Considered whether the directors have disclosed that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the company, whether it has been in place for the year under review, whether it is regularly reviewed by the Board. Further, we considered whether the explanations given by in the statement is consistent with our understanding.
5. Reviewed the other documentation prepared by or for the directors to support their Statement on Internal Control.
6. Obtained written representations from directors on matters material to the Statement on Internal Control when 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 Company'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 company.

BDO Partners

CHARTERED ACCOUNTANTS
Colombo 02

12th September, 2017
HA/um

BDO Partners, a Sri Lankan Partnership, is a member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.

Partners : Sujeewa Rajapakse FCA, FCMA, MBA. Tishan H. Subasinghe FCA, ACMA, CISA, MBA. H. Sasanka Rathnaweera FCA, ACMA.
Ashane J.W. Jayasekara FCA, FCMA (UK), MBA. Hasanthi D. Amarakoon ACA, ACMA. R. Vasanthakumar Bsc (Acc), ACA

Independent Auditors' Report

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TO THE SHAREHOLDERS OF MERCANTILE INVESTMENTS AND FINANCE PLC

Report on the Financial Statements

We have audited the accompanying financial statements of Mercantile Investments and Finance PLC, which comprise the statement of financial position as at 31st March, 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information as set out on pages 295 to 360.

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 the Board determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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 the 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 financial statements give a true and fair view of the financial position of Mercantile Investments and Finance PLC as at 31st March, 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 Company.
- The financial statements of the Company, comply with the requirements of section 151 of the Companies Act No.07 of 2007.

BDO Partners

CHARTERED ACCOUNTANTS
Colombo

12th September, 2017
HA/um

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Statement of Comprehensive Income

For the year ended 31st March	Note	2017 Rs.'000	2016 Rs.'000
Gross income	6	5,645,533	4,500,275
Interest income	7.1	5,286,060	4,301,828
Interest expenses	7.2	(3,136,218)	(2,098,378)
Net interest income		2,149,842	2,203,450
Fee and commission income	8	83,622	58,927
Net fee and commission income		83,622	58,927
Other operating income	9	275,851	139,520
Total operating income		2,509,315	2,401,897
Impairment charge/(reversal) for loans and receivables	10	(625,066)	(234,816)
Net operating income		1,884,249	2,167,081
Less: Operating expenses			
Personnel expenses	11	(678,232)	(532,029)
Depreciation and amortisation	12	(69,186)	(49,994)
Other operating expenses	13	(814,508)	(732,998)
Total operating expenses		(1,561,926)	(1,315,021)
Operating profit before value added tax and NBT on financial services		322,323	852,060
Value added tax and NBT on financial services		(112,838)	(141,090)
Operating profit after value added tax and NBT on financial services		209,485	710,970
Add: Share of associate company's profit before taxation	14	104,194	91,675
Profit before taxation from operations		313,679	802,645
Less: Income tax expenses	15	(111,665)	(297,626)
Profit for the year		202,014	505,019
Net other comprehensive income/(expenses)			
Other comprehensive income/(expenses) to be reclassified to profit or loss in subsequent periods			
Changes in fair value of available for sale financial assets (Note 44)		19,584	(655,757)
Other comprehensive income/(expenses) to be reclassified to profit or loss in subsequent periods		19,584	(655,757)
Net other comprehensive income/(expenses) not to be reclassified to profit or loss in subsequent periods			
Deferred tax effect on revaluations surplus on building (Note 37)		629	(16,092)
Share of other comprehensive income of associates		(5,183)	72,773
Actuarial gain/(loss) on retirement benefit obligations (Note 38)		(1,185)	(11,278)
Deferred tax effect on actuarial gain (Note 37)		(2,826)	844
Net other comprehensive income/(expenses) not to be reclassified to profit or loss in subsequent periods		(8,565)	46,247
Other comprehensive income/(expenses) for the year net of tax		11,019	(609,510)
Total comprehensive income/(expenses) for the year net of tax		213,033	(104,491)
Earnings per share			
Basic earnings per share (Rs.)	16	67.20	168.00
Diluted earnings per share (Rs.)	16	67.20	168.00
Dividend per ordinary share (Rs.)	17	-	7.00

Figures in brackets indicate deductions.

The significant accounting policies and the notes from pages 295 to 360 form an integral part of these financial statements.

Statement of Financial Position

As at 31st March	Note	2017 Rs.'000	2016 Rs.'000
Assets			
Cash and cash equivalents	20	1,244,554	344,062
Placement with banks	21	53,501	464,984
Financial investments - available for sale (quoted)	22	3,823,125	4,570,688
Loans and receivables	23	11,366,577	8,302,333
Finance leases receivables	24	11,093,954	9,925,519
Hire purchase receivables	25	6,184,745	6,825,676
Financial investments - available for sale (unquoted)	22	70,427	70,427
Other financial assets	26	445,786	110,440
Inventories	27	7,882	16,467
Other assets	28	81,732	72,414
Current tax refunds		121,051	27,212
Investment in associates	29	995,977	927,318
Investment property	30	158,340	448,234
Property, plant and equipment	31	1,790,296	1,803,939
Leasehold property	32	42,140	42,608
Intangible assets	33	12,577	12,386
Total assets		37,492,664	33,964,707
Liabilities			
Bank overdraft		1,092,434	412,472
Deposits due to customers	34	17,017,674	15,815,590
Debt instruments issued and other borrowings	35	10,165,837	8,527,169
Other financial liabilities	36	776,819	1,052,327
Deferred tax liabilities	37	361,223	343,259
Other liabilities		39,640	13,423
Retirement benefit obligations	38	171,772	146,235
Total liabilities		29,625,399	26,310,475
Shareholders' funds			
Stated capital	39	36,000	36,000
Revaluation reserve	40	1,535,061	1,539,615
Statutory reserve fund	41	661,400	631,400
General reserves	42	4,086,430	4,086,430
Retained earnings	43	1,291,730	1,123,727
Available for sale reserve	44	256,644	237,060
Total shareholders' funds		7,867,265	7,654,232
Total liabilities and shareholders' funds		37,492,664	33,964,707
Net assets per share (Rs.)		2,617	2,546
Capital commitments and contingencies	45 & 46		

The significant accounting policies and the notes from pages 295 to 360 form an integral part of these financial statements.

Certification
I certify that these financial statements have been prepared in compliance with the requirements of the Companies Act No. 07 of 2007.

Shermal H. Jayasuriya
Finance Director

The Board of Directors is responsible for the preparation and the presentation of these financial statements.
Approved and signed for and on behalf of the Board.

Gerard G. Ondaatjie
Managing Director

Angeline M. Ondaatjie
Director

Colombo
12th September, 2017

Statement of Changes in Equity

For the year ended 31st March	Stated capital	Revaluation reserves land and buildings	Associate company reserve	Statutory reserves	General reserves	Available for sale reserve	Retained earnings	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
As at 01st April, 2015	36,000	1,100,437	382,497	581,400	3,886,430	892,817	900,184	7,779,765
Total comprehensive income for the year								
Profit for the year	-	-	-	-	-	-	505,019	505,019
Other comprehensive income / (expenses)	-	(16,092)	72,773	-	-	(655,757)	(10,434)	(609,510)
Total comprehensive income /(expenses)	-	(16,092)	72,773	-	-	(655,757)	494,585	(104,491)
Dividends paid to equity shareholders	-	-	-	-	-	-	(21,042)	(21,042)
Transfer to statutory reserve	-	-	-	50,000	-	-	(50,000)	-
Transfer to general reserve	-	-	-	-	200,000	-	(200,000)	-
As at 31st March, 2016	36,000	1,084,345	455,270	631,400	4,086,430	237,060	1,123,727	7,654,232
Total comprehensive income for the year								
Profit for the year	-	-	-	-	-	-	202,014	202,014
Other comprehensive income/(expenses)	-	629	(5,183)	-	-	19,584	(4,011)	11,019
Total comprehensive income/(expenses)	-	629	(5,183)	-	-	19,584	198,003	213,033
Transfer to statutory reserve	-	-	-	30,000	-	-	(30,000)	-
Transfer to general reserve	-	-	-	-	-	-	-	-
As at 31st March, 2017	36,000	1,084,974	450,087	661,400	4,086,430	256,644	1,291,730	7,867,265

Figures in brackets indicate deductions.

The significant accounting policies and the notes from pages 295 to 360 form an integral part of these financial statements.

Statement of Cash Flows

Accounting Policy

The statement of cash flow has been prepared by using the "Direct Method", in accordance with Sri Lanka Accounting Standard – LKAS 7 on "Statement of Cash Flow" whereby gross cash receipts and gross cash payments of operating activities, finance activities, and investing activities have been recognised. Cash and cash equivalents include cash in hand, balances with banks and highly liquid investment instruments with an original maturity of three months or less as given in the note 20.

For the year ended 31st March		**2017**	**2016**
	Note	**Rs.'000**	**Rs.'000**
Cash flow from operating activities			
Interest and commission receipts		5,369,681	4,360,755
Interest payments		(3,136,218)	(2,098,378)
Cash receipts from customers		(145,788)	21,815
Cash payments to employees, suppliers and tax authority		(1,399,200)	(1,391,278)
Operating profit before changes in operating assets and liabilities (Note A)		688,475	892,914
(Increase) / decrease in operating assets			
Short term funds			
Deposits held for regulatory or monetary control purposes		934,075	(177,118)
Funds advanced to customers		(4,119,821)	(5,820,051)
Other short term negotiable securities		679,962	139,838
Other receivables		(336,249)	(41,777)
Increase / (decrease) in operating liabilities			
Other payables		1,202,085	501,412
Deposits from customers		(249,290)	2,094,861
		(1,200,763)	(2,409,921)
Income taxes paid		(173,757)	(248,156)
Net cash from operating activities		(1,374,520)	(2,658,077)
Cash flows from investing activities			
Dividends received		177,001	103,072
Dividends received from associates		14,370	14,239
Proceeds from sale of non-dealing securities and government securities		228,422	20,068
Purchase of non-dealing securities		(21,148)	19,019
Proceeds from sale of property, plant and equipment		326,054	50,076
Purchase of property, plant and equipment and investment property	30 & 31	(85,378)	(386,940)
Acquisition of intangible assets	33	(2,977)	(9,491)
Net cash from investing activities		636,344	(227,995)
Cash flows from financing activities			
Borrowings obtained during the year		15,543,701	12,329,545
Borrowings repaid during the year		(13,905,033)	(9,485,017)
Dividends paid		-	(21,042)
Net Cash from financing activities		1,638,668	2,823,486
Net increase in cash and cash equivalents		900,492	(62,586)
Cash and cash equivalents at the beginning of the period		344,062	406,648
Cash and cash equivalents at the end of the period (Note B)		1,244,554	344,062

Statement of Cash Flow

For the year ended 31st March		2017	2016
	Note	Rs.'000	Rs.'000
Reconciliation of profit before tax with cash inflow from operating activities (Note A)			
Profit before tax		313,679	802,645
Capital gain from sale of quoted shares and treasury bonds	9	(59,542)	(5,143)
Dividend from investing securities	9	(177,001)	(103,072)
Share of profit of associates	14	(104,194)	(91,675)
(Profit)/loss on sale of property, plant and equipment	9	(3,071)	(9,490)
Depreciation of property, plant and equipment and investment property	30 & 31	65,932	49,077
Amortisation of leasehold property	32	468	468
Amortisation of intangible assets	33	2,786	449
Provision for bad and doubtful debts	10	625,066	234,816
Retirement benefit provision	38.2	28,327	23,456
Retirement benefit paid	38.1	(3,975)	(8,617)
		688,475	892,914
Cash and cash equivalents at the end of the period (Note B)			
Cash in hand	20	998,666	239,161
Balance with bank	20	245,888	104,901
		1,244,554	344,062

Figures in brackets indicate deductions.

The significant accounting policies and the notes from pages 295 to 360 form an integral part of these financial statements.

Significant Accounting Policies

1. Reporting entity

1.1. Corporate information

Mercantile Investments and Finance PLC is a public limited liability company, listed on the Colombo Stock Exchange, incorporated on 15th June, 1964 and domiciled in Sri Lanka. It is a licensed finance company regulated under the Finance Business Act No. 42 of 2011. The Company was re-registered under the Companies Act No. 07 of 2007.The registered office of the Company is located at No. 236, Galle Road, Colombo 03.

The staff strength of the Company as at 31st March, 2017 was 883 (738 as at 31st March, 2016).

1.2. Principal activities and nature of operations

Company

The Company provides a comprehensive range financial services including accepting deposits, granting of loans, lease financing, hire purchase financing, fleet management and share trading.

Associates

The principle activity of the Company's associate, namely Nuwara Eliya Hotels Company PLC is engaged in the business of the hoteliering.

There were no significant changes in the nature of the principle activities of the Company and its associate during the financial year under review.

1.3. Parent enterprise and ultimate parent enterprise

The Company doesn't have an identifiable parent of its own.

1.4. Approval of financial statements by the Board of Directors

The financial statements of Mercantile Investments and Finance PLC for the year ended 31st March, 2017 (including comparatives) were approved and authorised for issue by the Board of Directors on 12th September, 2017.

2. Basis of preparation

This section provides a summary of significant accounting policies, judgements, estimates and assumptions used and other general accounting policies.

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

2.1. Statement of compliance

The financial statements of the Company have been prepared and presented in accordance with Sri Lanka Accounting Standards comprising SLFRS and LKAS (hereafter "SLFRS"), as issued by the Institute of Chartered Accountants of Sri Lanka and in compliance with the requirements of the Companies Act No. 07 of 2007 and Finance Business Act No. 42 of 2011 and amendments thereto, provide appropriate disclosure as required by Listing Rules of the Colombo Stock Exchange. These Sri Lanka Accounting Standards are available at www.casrilanka.com.

The Company did not adopt any inappropriate accounting treatments which are not in compliance with the requirements of the SLFRSs and regulations governing the preparation and presentation of the financial statements.

The formats used in the preparation of the financial statements and the disclosures made therein also comply with the specified format prescribed by the Central Bank of Sri Lanka for the preparation, presentation and publication of annual audited financial statements of licensed finance companies.

2.2. Responsibility for financial statements

The Board of Directors is responsible for the preparation and fair presentation of the financial statements of the Company as per the provision of the Companies Act No. 07 of 2007 and the Sri Lanka Accounting Standards.

The Board of Directors acknowledges their responsibility for the financial statements in the statement of financial position on page no. 291.

These financial statements include the following components:

- Statement of Comprehensive Income providing the information on the financial performance of the Company for the year under review (refer page 290).
- Statement of Financial Position providing the information on the financial position of the Company as at year end (refer page 291).
- A Statement of Changes in Equity depicting all changes in shareholders' equity during the year under review (refer page 292).
- Statement of Cash Flow providing the information on the users on the ability of the Company to generate cash and cash equivalents and the needs to utilisation of those cash flows (refer pages 293 to 294)
- Notes to the Financial Statements comprising accounting policies used and other explanatory information (refer pages 303 to 360).

2.3. Basis of measurement

The financial statements have been prepared on a historical cost basis, except for the following material items in the statement of financial position.

Items	Basis of measurement	Note No.
Available-for-sale financial investments	Fair value	22
Land and buildings	Stated at valuation	31
Defined benefit obligations	Liability for defined benefit obligations is recognised as the present value of the defined benefit obligation plus unrecognised actuarial gains, less unrecognised past service cost and unrecognised actuarial losses.	38

Significant Accounting Policies

2.4. Functional currency and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Company operates (the functional currency).

These financial statements are presented in Sri Lankan Rupees, which is the Company's functional and presentation currency except when otherwise indicated.

2.5. Presentation of financial statements

The assets and liabilities of the Company presented in its statement of financial position are grouped by nature and listed in an order that reflects their relative liquidity and maturity pattern. No adjustments have been made for inflationary factors affecting the financial statements. An analysis on recovery or settlement within 12 months after the reporting date (current) and more than 12 months after the reporting date (non-current) is presented in the Note 52 to the financial statements.

2.6. Materiality and aggregation

Each material class of similar items is presented separately in the financial statements .Items of dissimilar nature or function are presented separately unless they are immaterial as permitted by Sri Lanka Accounting Standards LKAS 1 "Presentation of Financial Statements".

2.7. Rounding

The amounts in the financial statements have been rounded –off to the nearest Rupees thousands, except where otherwise indicated as permitted by the Sri Lanka Accounting Standards LKAS 1 "Presentation of Financial Statements".

2.8. Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously. Income and expenses are not offset in the statement of comprehensive income, unless required or permitted by an Accounting Standards or Interpretation, and as specifically disclosed in the accounting policies of the Company.

2.9. Comparative information

Comparative information including quantitative, narrative and descriptive information is disclosed in respect of the previous period in the financial statements in order to enhance the understanding of the current period's financial statements and to enhance the inter period comparability. The presentation and classification of the financial statements of the previous year are amended, where relevant for better presentation and to be comparable with those of the current year.

2.10. Going concern basis of accounting

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

2.11. Significant accounting judgements, estimates and assumptions

The preparation of the Company's financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures, and the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods and thus the actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis and revisions to accounting estimates are recognised prospectively.

The most significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have most significant effect on the amounts recognised in the financial statements of the Company are as follows:

2.11.1. Fair value of financial instruments

When the fair value of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, their fair value is determined using valuation techniques including the discounted cash flow model. The inputs to these models are taken from observable markets where possible, but where this is not possible, a degree of judgement is required in establishing fair values. The judgements include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments. The valuation of financial instruments is described in more detail in the Note 19 to the financial statements.

2.11.2. Financial assets and liabilities classification

The accounting policies of the Company provide scope for assets and liabilities to be classified at inception into different accounting categories under certain circumstances. The classification of financial instrument is given in the Note 18 to the financial statements.

2.11.3. Impairment losses on loans and advances

The Company reviews its individually significant loans and advances at each reporting date to assess whether an impairment loss should be recorded in the statement of comprehensive income. In particular, management's judgement is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors and hence, actual results may differ, resulting in future changes to the provisions made.

Loans and Advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence, but the effects of which are not yet evident.

The collective assessment takes account of data from the loan portfolio (such as levels of arrears, credit utilisation, loan-to-collateral ratios, etc.), and judgements on the effect of concentrations of risks and economic data (including levels of unemployment, real estate prices indices, country risk and the performance of different individual groups).The impairment loss on loans and receivables is disclosed in more detail in the Note 10, 23, 24 and 25 to the financial statements.

2.11.4. Impairment of available for sale investments

The Company reviews its debt securities classified as available for sale investments at each reporting date to assess whether they are impaired. This requires similar judgement as applied to the individual assessment of loans and advances.

The Company also records impairment charges on available for sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is 'significant' or 'prolonged' requires judgement. In making this judgement, the Company evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investment is less than its cost. The impairment loss on equity investments is disclosed in more detail in the Note 10 to the financial statements.

2.11.5. Impairment of non-financial assets

Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions, conducted at arm's length observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the budget for the next five years and do not include restructuring activities that the Company is not yet committed to or significant future investments that will enhance the asset discount rate used for the discounted cash flow model as well as the expected future cash-inflows and the growth rate used for extrapolation purposes.

2.11.6. Deferred tax assets

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that future taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

2.11.7. Defined benefit obligations

The cost of defined benefit plans are determined using actuarial valuations. An actuarial valuation involves making various assumptions which may differ from actual developments in the future. These include the determination of the discount rate, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation and long-term nature, a defined benefit obligation is subject to significant uncertainty.

2.11.8. Useful economic lives of property, plant and equipment

The Company reviews the residual values useful lives and method of depreciation of property, plant and equipment at each reporting date. Judgement of the management is exercised in the estimation of these values, rates, methods and hence, they are subject to uncertainty.

2.11.9. Revaluation of property, plant and equipment

The Company measures land and buildings at revalued amounts. The Company engaged an independent professional valuer to assess fair value of land and buildings as at 31st March, 2015. The key assumptions used to determine the fair value of the land and buildings are provided in the Note 31.4 to the financial statements.

2.11.10. Provisions for liabilities, commitments and contingencies

The Company receives legal claims in the normal course of business. Management has made judgements as to the likelihood of any claim succeeding in making provisions. The time of concluding legal claims is uncertain, as is the amount of possible outflow of economic benefits. Timing and cost ultimately depends on the due processes in respective legal jurisdictions.

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in the financial statements, unless otherwise indicated.

3. Significant accounting policies – Recognition of assets and liabilities.

3.1. Financial instruments — Initial recognition, classification and subsequent measurement

3.1.1. Date of recognition

All financial assets and liabilities except "regular way trades" are initially recognised on the trade date, i.e., the date that the Company becomes a party to the contractual provisions of the instrument. "Regular way trades", means purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place. Those trades are initially recognised on the settlement date.

3.1.2. Initial measurement of financial instruments

The classification of financial instruments at initial recognition depends on their purpose and characteristics and the management's intention in acquiring them. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss as per the Sri Lanka Accounting Standard – LKAS 39 on "Financial Instrument :Recognition and Measurement".

Transaction cost in relation to financial assets and financial liabilities at fair value through profit and loss are dealt with through the statement of comprehensive income.

3.1.2.1. Day 1' Profit or Loss

When the transactions price differs from the fair value of other observable current market transactions in the same instruments, or based on a valuation technique shows variables include only data from observable markets, the Company immediately recognises the difference between the transaction price and fair value (a'Day1' profit or loss) in "interest income and personnel expenses". In cases where fair value is determined using data which is not observable, or when the instrument is recognised, The 'Day 1 loss' arising in the case of loans granted to employees at concessionary rates under uniformly applicable schemes is deferred and amortised using "Effective Interest Rates" (EIR) over the remaining service period of the employees or tenure of the loan whichever is shorter.

Significant Accounting Policies

3.1.3. Classification and subsequent measurement of financial assets

At inception a financial asset is classified into one of the following categories;

- » At fair value through profit or loss :
  - – Held for trading or
  - – Designated at fair value through profit or loss
- » Loans and receivables;
- » Held to maturity; or
- » Available-for-sale

The subsequent measurement of financial assets depends on their classification.

Details on different types of financial assets recognised on the statement of financial position are given in the Note 18 to the financial statements.

3.1.3.1. At fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held-for-trading and financial assets designated upon initial recognition at fair value through profit or loss which are discussed below:

3.1.3.1.1. Held-for-trading

Financial assets are classified as held for trading if they are acquired principally for the purpose of selling or repurchasing in the near term or holds as a part of a portfolio that is managed together for short-term profit or position taking. This category also includes derivative financial instruments entered into that are not designated as hedging instruments in hedge relationships as defined by the Sri Lanka Accounting Standard - LKAS 39 on 'Financial Instruments: Recognition and Measurement'.

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 is recorded in 'net trading income' according to the terms of the contract, or when the right to receive the payment has been established.

The Company has not designated any financial assets upon initial recognition as held for trading.

3.1.3.1.2. Designated at fair value through profit or loss

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

The Company has not designated any financial assets upon initial recognition as at fair value through profit or loss.

3.1.3.2. Loans and receivables

Loans and receivables include, loans and receivables, finance leases receivables, hire purchase receivables and placements with the bank.

Details of loans and receivables are given in following Notes to the financial statements.

Items	Note No.
Loans and receivables	23
Finance leases receivables	24
Hire purchase receivables	25
Placement with banks	21

3.1.3.3. Held-to-maturity

Held-to-maturity financial investments are non-derivative financial assets with fixed or determinable payments and fixed maturities, which has the intention and ability to hold-to-maturity. After initial measurement, held-to-maturity financial investments are subsequently measured at amortised cost using the EIR, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR. The amortisation is included in 'interest income' in the statement of comprehensive Income. The losses arising from impairment of such investments are recognised in the statement of comprehensive income in 'impairment charge/ reversal for loans and receivables'.

3.1.3.4. Available for sale financial investments

Details of financial investments – available for sale are given in the Note 22 to the financial statements.

3.1.3.5. Cash and cash equivalents

Details of cash and cash equivalents are given in the Note 20 to the financial statements.

3.1.4. Classification and subsequent measurement of financial liabilities

At inception a financial liability is classified into one of the following categories;

- » At fair value through profit or loss
  - – Held for trading; or
  - – Designated at fair value through profit or loss.
- » At amortised cost

The subsequent measurement of financial liabilities depends on their classification.

Details on different types of financial liabilities recognised on the statement of financial position are given in the Note 18 to the financial statements.

3.1.4.1. At fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designed upon initial recognition as at fair value through profit or loss.

The Company has not designated any financial liabilities upon initial recognition as at fair value through profit or loss.

3.1.4.2. Financial liabilities at amortised cost

Financial instruments issued by the Company that are not designated at fair value through profit or loss, are classified as liabilities under 'due to customers', 'debt securities issued' or 'subordinated term debts' as appropriate, where the substance of the contractual arrangement results in the Company having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of owned equity shares.

After initial recognition, such financial liabilities are subsequently measured at amortised cost using the EIR method. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included in 'interest expenses' in the statement of comprehensive income. Gain and losses too are recognised in the statement of comprehensive income when the liabilities are derecognised as well as through the EIR amortisation process.

Details of financial liabilities at amortised cost are given in the following Notes to the financial statements.

Items	Note No.
Deposits due to customers	34
Debts instruments issued and other borrowings	35

3.1.5. Reclassification of financial assets and liabilities

Reclassifications are recorded at fair value at the date of reclassification, which becomes the new amortised cost.

For a financial asset reclassified out of the 'available for sale' category, any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the EIR. Any difference between the new amortised cost and the expected cash flows is also amortised over the remaining life of the asset using the EIR. If the asset is subsequently determined to be impaired, then the amount recorded in equity is recycled to the statement of comprehensive income.

The Company may reclassify a non–derivative trading asset out of the 'held for trading' category and into the 'loans and receivables' category if it meets the definition of loans and receivables and the Company has the intention and ability to hold the financial asset for the foreseeable future or until maturity. If a financial asset is reclassified, and if the Company subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the EIR from the date of the change in estimate.

Reclassification is at the election of management, and is determined on an instrument by instrument basis. The Company does not reclassify any financial instrument into the fair value through profit or loss category after initial recognition.

3.1.6. De-recognition of financial assets and financial liabilities

3.1.6.1. Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

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

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

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

3.1.6.2. Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in the statement of comprehensive income.

3.1.7. Fair value of financial instruments

Fair value measurement of financial instruments including the fair value hierarchy is explained in the Note 19 to the financial statements.

3.1.8. Identification and measurement of impairment of financial assets

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

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

In addition, for an investment in an equity security a significant or prolonged decline in its fair value below its cost is considered as an objective evidence of impairment.

3.1.8.1. Impairment of financial assets carried at amortised cost

Details of the individual and collective assessment of impairments are given in the Note 10 to the financial statements.

3.1.8.2. Impairment of financial investments - available-for-sale

For available-for-sale financial investments, the Company assesses at each reporting date whether there is objective evidence that an investment is impaired.

In the case of equity investments classified as available for sale, objective evidence would also include a 'significant' or 'prolonged' decline in the fair value of the investment below its cost. A decline of 20%-40% of the fair value of an investment in an equity instrument below its acquisition cost may be considered

Significant Accounting Policies

as significant and a general stock market decline over a period of 12 months may not be necessarily considered as prolonged. However judgment is made after a careful analysis of the specific facts and circumstances of each case. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in equity through other comprehensive income is removed from equity and recognised in the statement of comprehensive income. Increases in the fair value after impairment are recognised in the other comprehensive income.

3.1.9. Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously. This is not generally the case with master netting agreements, therefore, the related assets and liabilities are presented gross in the statement of financial position.

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

3.2. Impairment of non-financial assets

The carrying amounts of the Company's non-financial assets, other than deferred tax assets are reviewed at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. Where the carrying amount of an asset or cash-generating unit exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded subsidiaries or other available fair value indicators. Impairment losses of continuing operations are recognised in the statement of comprehensive income under those expense categories consistent with the function of the impaired asset, except for property previously revalued where the gain or loss on revaluation was taken to equity. In this case, the impairment is also recognised in equity upto the extent of any previously recognised revaluation gains.

For assets, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Company estimates the asset's or cash-generating unit's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation/amortisation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of comprehensive income.

3.3. Leases

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

3.3.1. Operating leases

3.3.1.1. Operating leases – company as a lessee

Leases that do not transfer to the Company substantially all risks and benefits incidental to ownership of the leased assets are operating leases. Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight line basis over the lease term. Contingent rental payable is recognised as an expense in the period in which they are incurred.

The Company does not have any operating leases as a lessee.

3.3.1.2. Operating leases – company as a lessor

Leases where the Company does not transfer substantially all risks and benefits of ownership of the asset are classified as operating leases.

Details of 'operating leases' are given in the Note 9, 26 and 31 to the financial statements.

3.3.2. Finance leases

3.3.2.1. Finance leases – company as a lessee

Finance leases that transfer substantially all risks and benefits incidental to ownership of the leased item to the Company, are capitalised at the commencement of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability.

A leased asset is depreciated over the useful life of the asset. However, if there is no reasonable certainty that the Company will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the estimated useful life of the asset and the lease term.

The Company does not have any finance leases as a lessee.

3.3.2.2. Finance leases – company as a lessor

When the Company is the lessor under finance leases the amounts due under the leases, after deduction of unearned charges, are included in 'finance leases receivables'. The finance income receivable is recognised in 'interest income' over the periods of the leases so as to give a constant rate of return on the net investment in the leases.

Details of 'finance leases receivables' are given in the Note 24 to the financial statements.

3.4. Hire purchase receivable

Advances granted under agreements that transfer substantially all the risks and rewards associated with ownership other than legal title, are classified as "hire purchases receivables."

Details of hire purchase receivables are given in the Note 25 to the financial statements.

3.5. Property, plant and equipment

Details of property, plant and equipment are given in the Note 31 to the financial statements.

3.5.1. Depreciation

Details of depreciation are given in the Note 12 to the financial statements.

3.6. Intangible assets

Details of intangible assets are given in the Note 33 to the financial statements.

Amortisation recognised during the year in respect of intangible assets is included under the item of amortisation of intangible assets under depreciation and amortisation in the statement of comprehensive income.

3.7. Investment property

Details of investment property are given in the Note 30 to the financial statements.

3.8. Provisions

When the Company has a present obligation (legal or constructive) as a result of a past event, where it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and the Company can reliably estimate the amount of the obligation, we recognise it as a provision in accordance with LKAS 37 - Provisions, Contingent Liabilities and Contingent Asset.

3.9. Borrowing cost

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the respective asset. All other borrowing costs are expensed in the period in which they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

3.10. Employee benefits

3.10.1. Defined benefit plan – gratuity

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".

Details of retirement benefit obligations are given in the Note 38 to the financial statements.

3.10.2. Defined contribution plan

Details of the defined contribution plans and amount recognised in the statement of comprehensive Income as expenses on defined contribution plans are given in the Note 11 to the financial statements.

4. Significant accounting policies – recognition of income and expenses

Details and recognition criteria of income and expenses are given in the Notes 6 to 13 to the financial statements.

4.1. Income tax expenses

Details of income tax expense are given in the Note 15 to the financial statements.

5. New accounting standards issued but not yet effective

A number of new standards and amendments to standards, which have been issued but not yet effective as at the reporting date, have not been applied in preparing these financial statements. Accordingly, the following accounting standards have not been applied in preparing these financial statements and the Company plans to apply these standards on the respective effective dates.

Accounting Standard	Requirement	Possible impact on the financial statements
SLFRS 9 – 'Financial Instruments'	This standard will replace Sri Lanka Accounting Standard – LKAS 39 (Financial Instruments: Recognition and Measurements). The improvements introduced by SLFRS 9 includes a model for classification and measurement, a single, forward-looking 'expected loss' impairment model and a reformed approach to hedge accounting which are detailed below.	Given complexities and technical expertise required in the process of adopting SLFRS 09, the Company has completed the initial assessment and analysis stage during the year ended 31st March, 2017 with the assistance of an external consultant.
	SLFRS 9 will become effective on 01st January 2018. **Classification and measurement** SLFRS 9 provides an approach for the classification of financial assets driven by cash flow characteristic and the business model in which as asset is held. Accordingly, financial assets are measured at amortised cost, fair value through other comprehensive income ('FVOCI') on fair value through profit or loss ('FVPL'). The classification of financial liability is essentially unchanged.	Classification and measurement phase is currently being finalised. However, the Company is not expected to have a material impact from the new classification principles introduced by SLFRS 9.

Significant Accounting Policies

Accounting Standard	Requirement	Possible impact on the financial statements
	Impairment	
	SLFRS 9 introduces a new, expected loss impairment model that will require more timely recognition of expected credit losses. Specifically, the new standard requires entities to account for expected credit losses from when financial instruments are first recognised. These credit loss (impairment) requirements apply to financial assets measured at amortised cost and FVOCI, lease receivables and certain loan commitments and financial guarantee contracts. The impairment methodology under SLFRS 9 requires impairment to be assessed under 3 stages.	The Company expects to finalise the impairment calculation models and quantify the impairment provision for 2016 based SLFRS 9 by the end of September 2017.
	Stage 01	
	Under LKAS 39 the Company has been recording an allowance for "Incurred But Not Identified" (IBNI) impairment losses. These are designed to reflect impairment losses that had been incurred in the performing portfolio but have not been identified. Under SLFRS 9, the impairment of financial assets that are not considered to have suffered a significant increase in their credit risk will be measured on a 12-month ECL basis.	Currently the Company is in the process of identifying and implementing the most appropriate policy for determining 'default', 'significant increase in credit risk', 'exposure at default' and 'credit conversion factors' that are used to meet the requirements of ECL calculations. This requires alignment of existing credit risk policies with historical data for financial reporting purposes.
	Stage 02	
	SLFRS 9 requires financial assets to be classified in stage 2 when their credit risk has increased significantly since their initial recognition. For these assets, a loss allowance needs to be recognised based on their lifetime ECLs. Since this is a new concept compared to LKAS 39, it will result in increased allowance as most such assets are not considered to be credit-impaired under LKAS 39.	
	Stage 03	
	Financial assets will be included in stage 3 when there is objective evidence that the loan is credit impaired.	Loans in stage 3, where the Company calculated the LKAS 39 impairment on an individual basis are not expected to be significantly different, but collateral values will be adjusted to reflect the amounts that can be expected to be realised.
SLFRS 16 – 'Leases'	SLFRS 16 eliminates the classification of leases as either operating or finance for lessees and instead, introduce single lessee accounting model. This model reflects that leases result in a company obtaining the right to use an asset at the start of the lease and, because most lease payments are made over time, also obtaining financing. As a result, the new standard requires lessees to account for all of their leases in a manner similar to how finance leases were treated applying LKAS 17. SLFRS 16, supersedes the requirement in LKAS 17 leases and will become effective on 01st January, 2019.	The Company is assessing the potential impact on its financial statements resulting from the application of SLFRS 16.

The following new Accounting Standards are not expected to have a significant impact on the financial statements of the Company.

SLFRS 15 – Revenue from Contracts with Customers'– effective date – 01st January, 2017.

Notes to the Financial Statements

6. Gross Income

Accounting Policy

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and such revenue can be reliably measured. The specific recognition criteria is given under the respective income notes.

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Interest income (Note 7.1)	5,286,060	4,301,828
Fee and commission income (Note 8)	83,622	58,927
Other operating income (Note 9)	275,851	139,520
Total	5,645,533	4,500,275

7. Net Interest Income

Accounting Policy

Recognition of income and expense

For all financial instruments measured at amortised cost and interest bearing financial assets classified as available for sale, interest income or expense is recorded using the Effective Interest Rate (EIR). EIR is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability.

The calculation takes into account all contractual terms of the financial instrument (for example, pre-payment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Company revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded as 'interest and similar income' for financial assets and 'interest and similar expense' for financial liabilities.

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

Discounts/premium on treasury bills and treasury bonds are amortised over the period to reflect a constant periodic rate of return. The coupon interest on treasury bonds is recognised on an accrual basis. The interest income on securities purchased under resale agreements is recognised in the statement of comprehensive income on an accrual basis over the period of the agreement.

7.1 Interest Income

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Income from finance lease	1,873,991	1,317,611
Income from hire purchase	1,262,361	1,459,426
Income from other loans and receivables	1,919,319	1,395,042
Income from treasury bills and bonds	200,207	98,809
Income from fixed deposits	30,182	30,940
Total	5,286,060	4,301,828

7.2 Interest Expenses

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Interest on fixed deposits	1,841,797	1,423,019
Interest on savings deposits	4,564	3,492
Interest on certificate of deposits	648	2,165
Interest on bank overdraft	26,773	23,845
Interest on debts securities	5,301	8,311
Interest on bank, securitised borrowings and other financial assets at amortised cost	1,257,135	637,546
Total	3,136,218	2,098,378
Net interest income	2,149,842	2,203,450

Notes to the Financial Statements

8. Fee and Commission Income

Accounting Policy

The Company earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

Fee income earned from services that are provided over a certain period of time

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the purchase or sale of business is recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Service charges	83,622	58,927
Total	83,622	58,927

9. Other Operating Income

Accounting Policy

Other income

Other income is recognised on an accrual basis.

Dividend income

Dividend income is recognised when the Company's right to receive the payment is established.

Gain or losses on disposal of property, plant and equipment, investments in government securities, dealing securities and investment securities

Gains or losses resulting from the disposal of property, plant and equipment, investments in government securities, dealing securities and investment securities are accounted for on cash basis in the statement of comprehensive income, in the period in which the sale occurs.

Recovery of bad and doubtful debts written off

Recovery of amounts written off as bad and doubtful debts is recognised on a cash basis.

Operating lease rental income

Income arising on operating leases is accounted for on a straight line basis over the lease terms on ongoing leases.

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Capital gain from sale of quoted shares and treasury bonds	59,542	5,143
Dividend income	177,001	103,072
Rent income	16,120	14,842
Profit/(loss) on disposal of property, plant and equipment	3,071	9,490
Operating lease rental income	8,507	3,785
Other income	(1,871)	(2,130)
Bad debts recovered	13,481	5,318
Total	275,851	139,520

10. Impairment Charge/(Reversal) for Loans and Other Losses

Accounting Policy

The Company recognises the changes in the impairment provisions for loans and other losses which are assessed as per the LKAS 39 - "Financial Instruments - Recognition and Measurement". The methodology adopted by the Company is explained below:

Individual assessment of impairment

Individual assessment of impairment for financial assets carried at amortised cost (such as loans and advances to customers, finance leases and hire purchase receivable), the Company first assesses individually, whether objective evidence of impairment exists for financial assets that are individually significant or collectively for financial assets that are not individually significant. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of a provision account and the amount of impairment loss is recognised in the statement of comprehensive income. Interest income continues to be accrued and recorded in ‘interest income’ on the reduced carrying amount/impaired balance and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

The present value of the estimated future cash flows is discounted at the financial asset’s original EIR. The calculation of the present value of the estimated future cash flows of collateralised financial asset, reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

Loans together with the associated impairment provision are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Company. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the provision account. If a future write-off is later recovered, the recovery is credited to ‘other income’.

Collective assessment of impairment

If the Company determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Company’s internal credit grading system, that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment, are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the Company. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect and are directionally consistent with changes in related observable data from year-to-year such as changes in;

- Changes in unemployment rate
- Property prices
- Commodity prices
- Payment status
- Growth in Gross Domestic Production (GDP)
- Inflation rates
- Changes in laws and regulations
- Interest rates
- Recent lending portfolio growth and product mix

The methodology and assumptions used for estimating provision for impairment including assumptions for projecting future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Impairment of rescheduled loans and advances

Where possible, the Company seeks to reschedule loans and advances rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. In case of individually significant rescheduled credit facilities, once the terms have been renegotiated, any impairment is measured using the original EIR as calculated before the modification of terms and the loan/advance is no longer considered past due. The management continually reviews renegotiated loans and advances to ensure that all criteria are met and that future repayments are likely to occur.

Notes to the Financial Statements

10. Impairment charge/(reversal) for loans and other losses (Contd.)

Accounting Policy

Collateral valuation

The Company seeks to use collateral, where possible, to mitigate its risks on financial assets. The fair value of collateral is generally assessed, at a minimum at inception and based on the Company's annual reporting schedule.

To the extent possible, the Company uses active market data for valuing financial assets, held as collateral. Other financial assets which do not have a readily determinable market value are valued using models. Non-financial collaterals such as motor vehicles, real estate are valued based on data provided by third parties such as valuers and other independent sources.

Collateral repossessed

Repossessed collateral will not be taken into books of accounts unless the Company has taken those collaterals into its business operations.

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Charge/(reversal) to the Statement of Comprehensive Income on impairment		
- Loans and receivables (Note 23.4)	246,308	198,289
- Finance leases receivables (Note 24.4)	(25,807)	49,100
- Hire purchase receivables (Note 25.4)	(39,171)	(12,573)
- Impairment of available for sale investment and other investments	443,736	-
Total	625,066	234,816

11. Personnel expenses

Accounting Policy

Personnel expenses include salaries and bonus, terminal benefit charges and other related expenses.

Bonus

The provision for bonus is recognised when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made on the amount of the obligation.

Defined contribution plans - Employees' Provident Fund (EPF) and Employees' Trust Fund (ETF)

A defined contribution plan is a post employment benefit plan under which an entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods as defined in the 'Sri Lanka Accounting Standard LKAS 19 - Employee Benefits'.

The contribution payable to a defined contribution plan is in proportion to the services rendered to the Company by the employees and is recorded as an expense when they become due. Unpaid contributions are recorded as a liability.

The Company and the employees contribute 14% and 8% respectively on the salary of each employee to the Employees' Provident Fund where as the Company contributes 3% of the salary to the Employees' Trust Fund.

Defined benefit plan - gratuity

Defined benefit plan contribution are recognised in the statement of comprehensive income based on an actuarial valuation carried out for the gratuity liability in accordance with 'LKAS 19 - Employee Benefits'.

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Salary and bonus	551,747	419,724
Employer's contribution to EPF	65,710	51,815
Employer's contribution to ETF	14,046	11,036
Defined benefit plan (Note 38)	28,327	23,456
Other allowances and staff related expenses	18,402	25,998
Total	678,232	532,029

12. Depreciation and Amortisation

Accounting Policy

Depreciation of property, plant and equipment

Depreciation is recognised in the statement of comprehensive income on a straight-line basis over the estimated useful lives of each part of an item of property and equipment since this method most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Freehold land is not depreciated. The estimated useful lives are as follows:.

Class of assets	Depreciation % per annum	Estimated useful life
Buildings	1.33 - 2.5	40 - 75 Years
Plant and machinery	20	5 Years
Computer equipment	25	4 Years
Office equipment	10	10 Years
Furniture and fittings	10	10 Years
Fixtures	10	10 Years
Motor vehicles	10 - 16.67	6 - 10 Years
Office bicycles	10	10 Years
Tools	25	4 Years

The depreciation rates are determined separately for each significant part of an item of property, plant and equipment and commence to depreciate 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 the management.

Depreciation of an asset ceases at the earlier of the date that the asset is classified as held-for-sale or the date that the asset is derecognised. Depreciation methods, useful lives and residual values are reassessed at each reporting date and adjusted if appropriate.

All classes of property, plant and equipment together with the reconciliation of carrying amounts and accumulated depreciation at the beginning and at the end of the year are given in the Note 31 to the financial statements.

Depreciation of investment property

Investment property includes lands and buildings. Depreciation on buildings is recognised on a straight line basis over the estimated useful life of 40-75 years.

Amortisation of intangible assets

Intangible assets are amortised using the straight line method to write down the cost over its estimated useful economic lives as given below:

Class of assets	Depreciation % per annum	Estimated useful life
Computer software	20% - 50%	2 - 5 Years

The unamortised balances of intangible assets with finite lives are reviewed for impairment whenever there is an indication for impairment and recognised as expenses in the statement of comprehensive income to the extent that they are no longer probable of being recovered from the expected future benefits.

The reconciliation of carrying amounts and accumulated amortisation and impairment at the beginning and end of the year are given in the Note 33 to the financial statements.

Amortisation of leasehold property

Leasehold property includes a land on 99 years lease which is amortised over the lease period using the straight line method.

Notes to the Financial Statements

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Depreciation of investment property (Note 30)	2,795	2,435
Depreciation of property, plant and equipment (Note 31)	63,137	46,642
Amortisation of leasehold property (Note 32)	468	468
Amortisation of intangible assets (Note 33)	2,786	449
Total	69,186	49,994

The Company has reviewed the residual value and the useful lives of the assets as at 31st March, 2017 and there were no material changes with the previous year assessment. However, as a result of the reassessment, in 2015/2016 the depreciation charge for the current/future periods has been reduced to Rs. 46,266,837/-. Had the assets been carried at the original residual values and the useful lives, the depreciation charge would have been Rs.72,569,399/-.

13. Other Operating Expenses

Accounting Policy

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

Crop Insurance Levy (CIL)

As per the provision of Section 14 of the Finance Act No. 12 of 2013, the CIL was introduced with effect from 01st April, 2013 and is payable to the National Insurance Trust Fund.

Currently, the CIL is payable at 1% of the profit after tax and amount relevant for the year is accounted under "others" category of other operating expense.

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Directors' emoluments (Note 13.1)	59,491	53,628
Auditors' remuneration	1,570	1,430
Professional and legal expenses	11,433	13,776
Advertising and business promotion expenses	60,713	84,627
Insurance premium	41,410	33,946
Donations	1,031	6,064
Office and building maintenance	43,963	36,413
Computer equipment maintenance	9,925	12,141
Penalties (Note 13.2)	-	600
Others	584,972	490,373
Total	814,508	732,998

13.1 Directors' emoluments

Directors' emoluments represents the fees, salaries and allowances paid to both Executive and Non-Executive Directors of the Company.

13.2 Penalties

This comprise penalties imposed by the Central Bank of Sri Lanka for exceeding the investment limits stipulated in the Finance Companies (Investments) Direction No.07 of 2006 and for the delay in submission of a weekly return.

14. Share of Associates Company's Profit Before Taxation

Accounting Policy

Investment in associates are accounted by using the equity method in terms of the Sri Lanka Accounting Standard - LKAS 28 - Investment in Associate and Joint Ventures.

The Company's share of profit or loss of an associate is recognised in the statement of comprehensive income.

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Nuwara Eliya Hotels Co. PLC (Note 29.1)	104,194	91,675
Total	104,194	91,675

15. Income tax expenses

Accounting Policy

As per the Sri Lanka Accounting Standard - LKAS 12 on 'Income Taxes', tax expense (tax income) is the aggregate amount included in determination of profit or loss for the period in respect of current and deferred taxes. Income tax expense is recognised in the statement of comprehensive income except to the extent it relates to items recognised directly in equity or in other comprehensive income (OCI), in which case it is recognised in equity or in OCI.

Current taxation

Current tax assets and liabilities consist of amounts expected to be recovered from or paid to the taxation authorities in respect of the current as well as prior years. The tax rates and tax laws used to compute the amounts are those that are enacted or substantially enacted at the reporting date. Accordingly, provision for taxation is made on the basis of the accounting profit for the year as adjusted for taxation purposes in accordance with the provisions of the Inland Revenue Act No. 10 of 2006 and the amendments thereto.

Deferred taxation

Detailed disclosure of accounting policies and estimate of deferred tax are available in the note 37 to the financial statements.

Value added tax on financial services

The base for the computation of value added tax on financial services is the accounting profit before emoluments paid to employees and income tax, which is adjusted for the depreciation computed on prescribed rates. The amount of value added tax charged in determining the profit or loss for the period is given in the statement of comprehensive income on page 290.

Nation building tax on financial services

The base for the computation of nation building tax on financial services is the accounting profit before emoluments paid to employees and income tax, which is adjusted for the depreciation computed on prescribed rates. The amount of nation building tax charged in determining the profit or loss for the period is given in the statement of comprehensive income on page 290.

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Income tax expenses on profit for the year (Note 15.1)	84,765	161,946
(Over)/ under provision in respect of previous year	11,133	29,270
Deferred tax (reversal)/ charged (Note 37)	15,767	106,410
Total	111,665	297,626

Notes to the Financial Statements

15.1 Reconciliation of Accounting Profit to Income Tax Expense

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Profit before tax	313,679	802,645
Add: Tax effect on non-deductible expenses	3,687,056	2,861,589
Less: Tax effect on deductible expenses	(3,414,346)	(3,039,328)
Tax effect on exempt income/profit	(340,736)	(108,215)
Assessable income	245,653	516,691
Taxable income	245,653	516,691
Income tax expense @ 28%	68,783	144,674
Share of income tax of associates (Note 29.1)	15,982	17,272
	84,765	161,946
Effective tax rate (excluding deferred tax)	27.02%	20.18%

The Company is liable for income tax at 28% on the taxable income for the current year (2016 - 28%).

The Company has taken into account the full benefit of capital allowances arising in terms of Section 23 of the Inland Revenue Act No. 10 of 2006 and amendments thereto in determining the taxation on profits for the year.

The Company's land and buildings have been revalued in the financial year 2014/2015 resulting in book values being written up by Rs.261,556,000/- of which Rs.190,623,000/- is related to land and this surplus if realised would not be liable to income tax.

15.2. Notional Tax Credit for Withholding Tax on Government Securities on Secondary Market Transactions

The Inland Revenue Act No 10 of 2006 and the amendments thereto, provide that a company which earns interest income from the secondary market transaction in government securities (earned on or after 01st April, 2002) would be entitled to a notional tax credit (being one - ninth of the net interest income), provided such interest income forms part of statutory income of the Company for that year of assessment.

Accordingly, the net interest income earned by the Company on the secondary market transaction in government securities for the year, has been grossed up in the financial statements and the resulting notional tax credit amounted to Rs.19,917,243/- (Rs. 9,880,879/- in 2016).

16. Basic/ diluted earnings per ordinary share

Accounting Policy

Basic earnings per share is calculated by dividing the net profit for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year, as required by the LKAS No 33 on Earning Per Share. The weighted average number of ordinary shares outstanding during the year and the previous year are adjusted for events that have changed the number of ordinary shares outstanding, without a corresponding change in the resources such as a bonus issue.

Diluted earnings per share is calculated by dividing the net profit attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year (adjusted for the effects all dilutive potential ordinary shares).

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Amount used as the numerator		
Net profit attributable to equity holders of the Company	202,014	505,019
Net profit attributable to equity holders of the Company for basic and diluted earnings per share	202,014	505,019

For the year ended 31st March	2017	2016
	Nos.'000	Nos.'000
Number of ordinary shares used as the denominator		
Weighted average number of ordinary shares	3,006	3,006
Weighted average number of ordinary shares used for basic and diluted earnings per share	3,006	3,006
Basic earnings per share (Rs.)	67.20	168.00
Diluted earnings per share (Rs.)	67.20	168.00

17. Dividend per ordinary share

Accounting Policy

Provision for final dividends is recognised at the time the divided recommended and declared by the Board of Directors, is approved by the shareholders. Interim dividend payable is recognised when the Board approves such dividend in accordance with the Companies Act No. 07 of 2007.

For the year ended 31st March	2017			2016		
	Gross dividend	Dividend tax	Net dividend	Gross dividend	Dividend tax	Net dividend
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
1st interim dividend						
Out of dividend received - free of tax	-	-	-	21,042	-	21,042
Out of normal profits	-	-	-	-	-	-
Total dividend	-	-	-	21,042	-	21,042
2nd interim dividend						
Out of dividend received - free of tax	-	-	-	-	-	-
Out of normal profits	-	-	-	-	-	-
Total dividend	-	-	-	-	-	-
Total	-	-	-	21,042	-	21,042
Dividend per ordinary share (Rs.)	-			7.00		

18. Analysis of financial instruments by measurement basis

Accounting Policy

Financial instruments are measured on an ongoing basis either at fair value or at amortised cost .The summary of significant accounting policies describes how the classes of financial instruments are measured and how income and expense, including fair value gains and losses are recognised. The following table analyses the carrying amounts of the financial instruments by category as defined in LKAS 39 - Financial Instruments : Recognition and Measurement and by headings of the statement of financial position.

Notes to the Financial Statements

18.1. Analysis of financial instrument by measurement basis as at 31.03.2017

	Held for trading (HFT)	Held to maturity (HTM)	Loans and receivables (L & R)	Available for sale (AFS)	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Financial assets					
Cash and cash equivalents	-	-	1,244,554	-	1,244,554
Placements with bank	-	-	53,501	-	53,501
Financial investments - available for sale	-	-	-	3,893,552	3,893,552
Loans and receivables	-	-	11,366,577	-	11,366,577
Finance leases receivables	-	-	11,093,954	-	11,093,954
Hire purchase receivables	-	-	6,184,745	-	6,184,745
Other financial assets	-	-	445,786	-	445,786
Total financial assets	-	-	30,389,117	3,893,552	34,282,669

	Fair value through profit or loss (FVTPL)	At amortised cost	Total
	Rs.'000	Rs.'000	Rs.'000
Financial liabilities			
Bank overdraft	-	1,092,434	1,092,434
Deposits due to customers	-	17,017,674	17,017,674
Debt instruments issued and other borrowed funds	-	10,165,837	10,165,837
Other financial liabilities	-	776,819	776,819
Total financial liabilities	-	29,052,764	29,052,764

18.2 Analysis of financial instrument by measurement basis as at 31.03.2016

	Held for trading (HFT)	Held to maturity (HTM)	Loans and receivables (L & R)	Available for sale (AFS)	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Financial assets					
Cash and cash equivalents	-	-	344,062	-	344,062
Placements with bank	-	-	464,984	-	464,984
Financial investments - available for sale	-	-	-	4,641,115	4,641,115
Loans and receivables	-	-	8,302,333	-	8,302,333
Finance leases receivables	-	-	9,925,519	-	9,925,519
Hire purchase receivables	-	-	6,825,676	-	6,825,676
Other financial assets	-	-	110,440	-	110,440
Total financial assets	-	-	25,973,014	4,641,115	30,614,129

	Fair value through profit or loss (FVTPL) Rs.'000	At amortised cost Rs.'000	Total Rs.'000
Financial liabilities			
Bank overdraft	-	412,472	412,472
Deposits due to customers	-	15,815,590	15,815,590
Debt instruments issued and other borrowed funds	-	8,527,169	8,527,169
Other financial liabilities	-	1,052,327	1,052,327
Total financial liabilities	-	25,807,558	25,807,558

19. 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.

The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. External valuers are involved for valuation of significant assets such as properties.

19.1. Determination of fair value and fair value hierarchy

For all financial instruments where fair values are determined by referring to externally quoted price or observable pricing inputs to models, independent price determination or validation is obtained. In an inactive market, direct observation of a trade price may not be possible. In these circumstances the Company uses alternative market information to validate the financial instrument's fair value with greater weight given to information that is considered to be more relevant and reliable.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised using the following fair value hierarchy, which reflects the significance of the inputs used in the fair value measurement.

Fair values hierarchy

Level 1 - Quoted market price (unadjusted) : financial instruments with the quoted prices in active markets.

Level 2 - Valuation technique using observable inputs : financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments are valued using models where all significant inputs are observable.

Level 3 - Valuation technique with significant unobservable inputs : financial instruments are valued using valuation techniques where one or more significant inputs are unobservable.

19.2. Valuation framework

The Company has established control framework with respect to the measurement of fair values of all significant assets and liabilities.

Specific controls include

* Review and approval process for significant judgements and assumptions

* Periodic review of fair value measurements against observable market data

Notes to the Financial Statements

19.3. Assets and liabilities measured at fair value and fair value hierarchy

The following table provides an analysis of assets and liabilities measured at fair value as at the reporting date, by the level in the fair value hierarchy into which the fair value measurement is categorised. These amount were based on the values recognised in the statement of financial position.

As at 31st March	2017				2016			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000
Non- financial assets								
Property, plant and equipment								
Land and buildings (Note 19.3.1)	-	-	1,445,021	1,445,021	-	-	1,444,100	1,444,100
	-	-	1,445,021	1,445,021	-	-	1,444,100	1,444,100
Financial assets								
Financial investments- available for sale								
Quoted investments	3,054,220	-	-	3,054,220	3,292,519	-	-	3,292,519
Unquoted investments (Note 19.3.2)	-	-	70,427	70,427	-	-	70,427	70,427
Government debt securities	758,750	-	-	758,750	1,267,769	-	-	1,267,769
Corporate debts securities	10,200	-	-	10,200	10,400	-	-	10,400
	3,823,125	-	70,427	3,893,552	4,570,688	-	70,427	4,641,115

19.3.1. The fair value of the land and buildings are based on the valuation done by professionally qualified independent professional valuer on 31st March, 2015 and there is no material change in the fair values as at 31.03.2017 as per the management judgement.

19.3.2. Value of unquoted shares as at 31st March, 2017 categorised under financial investments available for sale whose fair values can not be reliably measured is stated at cost in the statement of financial position as permitted by the Sri Lanka Accounting Standard - LKAS 39 on Financial Instruments: Recognition and Measurement.

19.3.3. Significant unobservable inputs used in level 3 measurement

Note No 31.4 to the financial statements provides information on significant unobservable inputs used in measuring fair value of land and buildings categorised as level 3 in the fair value hierarchy.

There were no transfer between level 1 and level 2 during the year 2016 and 2017.

19.4. Financial instruments not measured at fair value and fair value hierarchy

The methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the statement of financial position are as follows:

19.4.1. Assets for which fair value approximates carrying value

For financial assets and liabilities that have a short term maturity it is assumed that carrying amount approximate their fair value. This assumption is also applied to savings accounts which doesn't have specific maturity.

19.4.2. Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated based on the discounted cash flow approach. This approach employs the current market interest rate of similar financial instruments as a significant unobservable input in measuring the fair value and accordingly, categorised under level 3 in the fair value hierarchy.

19.4.3. Sensitivity of significant unobservable inputs used to measure fair value of fixed rate financial instruments

A significant increase/(decrease) in the market interest rate would result in lower/(higher) fair value being disclosed.

19.4. Financial instruments not measured at fair value and fair value hierarchy (Contd...)

19.4.4. The following table shows the fair values of financial assets and liabilities not measured at fair value and related fair value hierarchy.

As at 31st March	2017					2016				
	Level 1	Level 2	Level 3	Total fair value	Total carrying amount	Level 1	Level 2	Level 3	Total fair value	Total carrying amount
	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000
Financial assets										
Cash and cash equivalents	-	-	-	1,244,554	1,244,554	-	-	-	344,062	344,062
Placement with banks	-	-	-	53,501	53,501	-	-	-	464,984	464,984
Loans and receivables	-	-	11,366,577	11,366,577	11,366,577	-	-	8,376,878	8,376,878	8,302,333
Finance leases receivables	-	-	11,093,954	11,093,954	11,093,954	-	-	9,843,026	9,843,026	9,925,519
Hire purchase receivables	-	-	6,184,745	6,184,745	6,184,745	-	-	6,780,973	6,780,973	6,825,676
Other financial assets	-	-	445,786	445,786	445,786	-	-	110,440	110,440	110,440
Total financial assets	-	-	29,091,062	30,389,117	30,389,117	-	-	25,111,317	25,920,363	25,973,014
Financial liabilities										
Bank overdraft	-	-	-	1,092,434	1,092,434	-	-	-	412,472	412,472
Deposits due to customers	-	-	17,017,674	17,017,674	17,017,674	-	-	15,737,921	15,737,921	15,815,590
Borrowings	-	-	10,165,837	10,165,837	10,165,837	-	-	8,527,169	8,527,169	8,527,169
Other financial liabilities	-	-	776,819	776,819	776,819	-	-	1,052,327	1,052,327	1,052,327
Total financial liabilities	-	-	27,960,330	29,052,764	29,052,764	-	-	25,317,417	25,729,889	25,807,558

19.5 Reclassification of financial assets

There have been no reclassification during the year 2016 and 2017

20. Cash and Cash Equivalents

Accounting Policy

Cash and cash equivalents comprise cash in hand, balances with banks, money at call and short notice that are subject to an insignificant risk of changes in their value. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

There were no cash and cash equivalents held by the Company that were not available for use by the Company.

Details of cash and cash equivalents in the statement of financial position are given below:

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Cash in hand	998,666	239,161
Balances with the banks	245,888	104,901
Total	1,244,554	344,062

As at 31st March, 2017, the Company had available Rs.1,629 Mn (2016-Rs.714 Mn) of undrawn committed borrowing facilities.

21. Placement with Banks

Accounting Policy

Balances with banks and financial institutions includes fixed deposits. Balances with banks and financial institutions are carried at amortised cost in the statement of financial position.

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Fixed deposits	53,501	464,984
Total	53,501	464,984

Notes to the Financial Statements

22. Financial Investments - Available For Sale

Accounting Policy

Available for sale financial investments include equity and debt securities. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated at fair value through profit or loss. Debt securities in this category are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity or in response to changes in the market conditions.

The Company has not designated any loans or receivables as available for sale. After initial measurement, available for sale financial investments are subsequently measured at fair value.

Unrealised gains and losses are recognised directly in equity through other comprehensive income in the ‘available for sale reserve’. When the financial investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the statement of comprehensive income in ‘other operating income’. Where the Company holds more than one investment in the same security, they are deemed to be disposed of on a first-in first-out basis. Interest earned whilst holding available for sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available for sale financial investments are recognised in the statement of comprehensive income as ‘other operating income’ when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the statement of comprehensive income in ‘impairment losses on financial investments’ and removed from the ‘available for sale reserve’.

Impairment of Available-for-sale financial investments

For available for sale financial investments, the Company assesses at each reporting date whether there is objective evidence that an investment is impaired.

In the case of equity investments classified as available for sale, objective evidence would also include a ‘significant’ or ‘prolonged’ decline in the fair value of the investment below its cost. A decline of 20% - 40% of the fair value of an investment in an equity instrument below acquisition cost may be considered as significant and a general stock market decline over a period of 12 months not be necessarily considered as prolonged. However, judgement is made after careful analysis of the specific facts and circumstances of each case. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in equity through other comprehensive income is removed from equity and recognised in the statement of comprehensive income. Increases in the fair value after impairment are recognised in other comprehensive income.

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Government securities and quoted investments		
Government debt securities	758,705	1,267,769
Equities (Note 22.1)	3,054,220	3,292,519
Corporate debt securities (Note 22.2)	10,200	10,400
	3,823,125	4,570,688
Unquoted investments		
Equities (Note 22.3)	70,427	70,427
	70,427	70,427
Total financial investments - available-for-sale	3,893,552	4,641,115

22.1 Equities (quoted)

As at 31st March	2017			2016		
	No of shares	Cost	Market value	No of shares	Cost	Market value
		Rs. '000	Rs. '000		Rs. '000	Rs. '000
Banks, finance and insurance						
Commercial Bank of Ceylon PLC	10,661,077	1,354,880	1,390,204	10,509,737	1,335,963	1,318,972
Lanka Orix Finance PLC	100,000	1,213	220	100,000	1,213	280
LB Finance PLC	-	-	-	1,746,148	161,810	185,266
Sampath Bank PLC	23,792	6,490	6,162	22,020	6,065	4,977
Singer Finance PLC	400,000	19,351	6,840	400,000	19,351	7,240
Vallibel Finance PLC	-	-	-	50,000	2,463	2,685
		1,381,934	1,403,426		1,526,865	1,519,420
Diversified holdings						
Aitken Spence & Co. PLC	15,000	343	843	15,000	343	1,103
John Keells Holding PLC	1,314,307	243,096	181,243	1,150,019	243,096	170,203
Richard Pieris & Co. PLC	16,035,995	96,582	133,099	16,035,995	96,582	115,459
Vallibel One PLC	5,176,000	144,896	90,580	5,176,000	144,896	92,133
		484,917	405,765		484,917	378,898
Hotels and travels						
Amaya Leisure PLC	928,800	58,466	59,257	903,000	56,660	54,632
Eden Hotels PLC	1,049,600	17,738	11,441	1,049,600	17,738	16,794
The Fortress Resorts PLC	100,000	2,844	1,160	100,000	2,844	1,300
Hotel Sigiriya PLC	38,900	1,620	3,785	38,900	1,620	3,734
John Keells Hotels PLC	13,000,000	209,107	130,000	13,000,000	209,107	156,000
Light House Hotels PLC	7,736,677	224,407	379,097	7,736,677	224,407	409,270
Mahaweli Reach Hotel PLC	507,000	20,467	9,633	507,000	20,467	11,458
Palm Garden Hotel PLC	200,000	25,913	4,820	200,000	25,913	5,980
Royal Palms Beach Hotels PLC	8,576,700	124,582	187,830	8,576,700	124,582	261,589
Tangerine Beach Hotels PLC	3,899,644	26,343	232,029	3,899,644	26,343	260,106
		711,487	1,019,052		709,681	1,180,863
Investment trust						
Lanka Century Investments PLC	61,800	7,157	649	61,800	7,157	618
		7,157	649		7,157	618
Manufacturing						
Royal Ceramic PLC	550,000	89,930	65,450	550,000	89,930	55,055
		89,930	65,450		89,930	55,055
Power & energy						
Lanka IOC PLC	118,500	5,308	3,437	118,500	5,308	3,851
		5,308	3,437		5,308	3,851
Land & property development						
East West Properties PLC	50,000	2,471	705	50,000	2,471	675
Seylan Development PLC	-	-	-	375,000	4,607	4,575
		2,471	705		7,078	5,250
Motor						
United Motors PLC	150,000	18,701	11,700	150,000	18,701	12,450
		18,701	11,700		18,701	12,450
Telecommunication						
Dialog Axiata PLC	11,000,000	118,130	124,300	11,000,000	118,130	112,200
		118,130	124,300		118,130	112,200
Construction & engineering						
Colombo Dockyard PLC	161,000	44,966	12,236	161,000	44,966	17,404
		44,966	12,236		44,966	17,404
Trading						
Odel PLC	300,000	11,943	7,500	300,000	11,943	6,510
		11,943	7,500		11,943	6,510
Total		2,876,944	3,054,220		3,024,676	3,292,519

Notes to the Financial Statements

22.2 Corporate debt securities

As at 31st March	2017			2016		
	No of shares	Cost	Market value	No of shares	Cost	Market value
		Rs. '000	Rs. '000		Rs. '000	Rs. '000
Debentures - Sampath Bank PLC	-	10,000	10,200	-	10,000	10,400
Total	-	10,000	10,200	-	10,000	10,400

22.3 Equities (non-quoted)

As at 31st March	2017			2016		
	No of shares	Cost	Market value	No of shares	Cost	Market value
		Rs. '000	Rs. '000		Rs. '000	Rs. '000
Security Ceylon (Pvt) Ltd	250	200	200	250	200	200
Credit Bureau of Sri Lanka	269	27	27	269	27	27
Finance Houses Consortium	20,000	200	200	20,000	200	200
Fair View Hotels (Pvt) Ltd	7,000,000	70,000	70,000	7,000,000	70,000	70,000
Total		70,427	70,427		70,427	70,427

All unquoted available for sale equity investments are recorded at cost since the fair value of these investments cannot be reliably measured.

There is no market for these investments and company intends to hold them in the long term.

Investment in ordinary shares of Commercial Bank of Ceylon PLC as at 31st March, 2017 represents 18% of the capital funds of the Company as shown in the last audited statement of financial position which exceeded the limit of 5% stipulated in the Section 2 (ii) of Finance Companies (Investments) Direction No. 07 of 2006 issued by the Central Bank of Sri Lanka.

Further, aggregate amount invested in ordinary shares of quoted, unquoted and associate companies represents 40% of the capital funds of the Company as shown in the last audited statement of financial position which exceeded the limit of 25% stipulated in the Section 2 (iii) of the Finance Companies (Investments) Direction No. 07 of 2006 issued by the Central Bank of Sri Lanka.

The Board of Directors requested additional time and expects to dispose the excess value over the limit once the share prices improve in the share market. Based on CBSL letter dated 04th May, 2017, MI was granted an extension till 31st May 2017. However, company was able to dispose the excess investment after the balance sheet date.

23. Loans and receivables

Accounting Policy

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

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

After initial measurement, 'loans and receivables' are subsequently measured at amortised cost using the EIR, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortisation is included in 'interest income' in the statement of comprehensive income. The losses arising from impairment are recognised in the statement of comprehensive income in "impairment charge/reversal for loans and receivables".

"Day 1" difference for staff loans

All staff loans granted at below market interest rates were recognised at fair value. The difference between the fair value and the amount disbursed were treated as 'day 1' difference and amortised as staff cost over the loan period by using effective interest rate (EIR). The staff loans were subsequently measured at amortised costs.

Write-off of loans and receivables

Loans (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is non-realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security.

As at 31st March	2017 Rs.'000	2016 Rs.'000
Gross loans and receivables	14,143,575	10,335,677
Prepaid rentals	(839)	(1,114)
Unearned interest	(2,243,224)	(1,745,292)
Allowance for impairment (Note 23.4)	(532,935)	(286,938)
Net loans and receivables	11,366,577	8,302,333

As at 31st March	2017 Rs.'000	2016 Rs.'000
23.1 Loans and receivables-within one year		
Gross loans and receivables	7,095,793	5,543,855
Prepaid rentals	(64)	-
Unearned interest	(1,164,391)	(919,701)
Loans and receivables	5,931,338	4,624,154
23.2 Loans and receivables-from one to five years		
Gross loans and receivables	7,039,022	4,781,628
Prepaid rentals	(775)	(1,114)
Unearned interest	(1,076,787)	(824,812)
Loans and receivables	5,961,460	3,955,702
23.3 Loans and receivables-after five years		
Gross loans and receivables	8,760	10,194
Unearned interest	(2,046)	(779)
Loans and receivables	6,714	9,415
23.4 Movement in allowance for impairment		
Balance at the beginning of the year	286,938	93,283
Bad debt written off during the year	(311)	(4,634)
Charge/(reverse) to the statement of comprehensive income	246,308	198,289
Balance at the end of the year	532,935	286,938
23.4.1 Individual impairment		
Balance at the beginning of the year	224,494	75,889
Bad debt written off during the year	(311)	(4,634)
Charge/(reverse) to the statement of comprehensive income	227,488	153,239
Balance at the end of the year	451,671	224,494
23.4.2 Collective impairment		
Balance at the beginning of the year	62,444	17,394
Bad debt written off during the year	-	-
Charge/(reverse) to the statement of comprehensive income	18,820	45,050
Balance at the end of the year	81,264	62,444

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As at 31st March	2017 Rs.'000	2016 Rs.'000
23.5 Sector wise analysis of loans and receivables		
Agriculture	222,669	174,786
Industrial	344,631	207,643
Tourism	202,435	83,217
Trading	3,332,683	2,464,906
Construction	399,817	650,978
Services	6,939,942	5,074,495
Others	2,701,398	1,679,652
Total	14,143,575	10,335,677

24. Finance leases receivables

Accounting Policy

When the Company is the lessor in a lease agreement that transfers substantially all the risks and rewards incidental to ownership of the asset to the lessee, the arrangement is classified as finance lease. Amount receivable under finance leases net of initial rentals received, unearned interest and provision for impairment are classified as finance leases receivables in the statement of financial position.

After initial measurement, 'finance leases receivables' are subsequently measured at amortised cost using the EIR, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortisation is included in 'interest income' in the statement of comprehensive income. The losses arising from impairment are recognised in the statement of comprehensive income in 'impairment charge/reversal for loans and receivables'.

As at 31st March	2017 Rs.'000	2016 Rs.'000
Gross finance leases receivables	14,578,343	12,948,251
Prepaid rentals	(2,849)	(3,318)
Unearned interest	(3,326,978)	(2,837,460)
Allowance for impairment (Note 24.4)	(154,562)	(181,954)
Net finance leases receivables	11,093,954	9,925,519

As at 31st March	2017 Rs.'000	2016 Rs.'000
24.1 Finance leases receivable-within one year		
Gross finance leases receivables	5,070,534	4,353,852
Prepaid rentals	(1,045)	(456)
Unearned interest	(1,660,452)	(1,384,367)
Finance leases receivables	3,409,037	2,969,029
24.2 Finance leases receivable-from one to five years		
Gross finance leases receivables	9,507,654	8,591,847
Prepaid rentals	(1,809)	(2,862)
Unearned interest	(1,666,522)	(1,453,011)
Finance leases receivables	7,839,323	7,135,974
24.3 Finance leases receivable-after five years		
Gross finance leases receivables	155	2,552
Unearned interest	(3)	(82)
Finance leases receivables	152	2,470

As at 31st March	2017 Rs.'000	2016 Rs.'000
24.4 Movement in allowance for impairment		
Balance at the beginning the year	181,954	193,202
Bad debt written off during the year	(1,585)	(60,348)
Charge/(reverse) to the statement of comprehensive income	(25,807)	49,100
Balance at the end of the year	154,562	181,954
24.4.1 Movement in individual impairment		
Balance at the beginning of the year	72,988	116,611
Bad debt written off during the year	(1,585)	(60,348)
Charge/(reverse) to the statement of comprehensive income	(2,441)	16,725
Balance at the end of the year	68,962	72,988
24.4.2 Movement in collective impairment		
Balance at the beginning of the year	108,966	76,591
Bad debt written off during the year	-	-
Charge/(reverse) to the statement of comprehensive income	(23,366)	32,375
Balance at the end of the year	85,600	108,966
24.5 Sector wise analysis of finance leases receivables		
Agriculture	682,155	611,404
Industrial	332,533	330,278
Tourism	366,414	271,109
Trading	2,565,520	2,592,583
Construction	99,980	93,506
Services	7,757,011	6,597,532
Others	2,774,730	2,451,839
Total	14,578,343	12,948,251

25. Hire purchases receivables

Accounting Policy

Advances granted under agreement that transfer substantially all the risks and rewards associated with ownership other than legal title, are classified as hire purchase receivables. Amount receivable under hire purchases net of initial rental received, unearned interest and provision for impairment are classified as hire purchases receivable in the statement of financial position.

After initial measurement, 'hire purchases receivables' are subsequently measured at amortised cost using the EIR, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortisation is included in 'interest income' in the statement of comprehensive income. The losses arising from impairment are recognised in the statement of comprehensive income in "impairment charge/ reversal for loans and receivables".

As at 31st March	2017 Rs.'000	2016 Rs.'000
Gross hire purchases receivables	8,196,266	8,837,042
Prepaid rentals	(1,226)	(1,226)
Unearned interest	(1,759,895)	(1,708,145)
Allowance for impairment (Note 25.4)	(250,400)	(301,995)
Net hire purchases receivables	6,184,745	6,825,676

Notes to the Financial Statements

As at 31st March	2017 Rs.'000	2016 Rs.'000
25.1 Hire purchases receivable-within one year		
Gross hire purchases receivables	3,264,507	3,907,022
Prepaid rentals	(155)	(135)
Unearned interest	(929,179)	(964,013)
Hire purchases receivables	2,335,173	2,942,874
25.2 Hire purchases receivable-from one to five years		
Gross hire purchases receivables	4,931,759	4,919,553
Prepaid rentals	(1,071)	(1,091)
Unearned interest	(830,716)	(743,594)
Hire purchases receivables	4,099,972	4,174,868
25.3 Hire purchases receivable-after five years		
Gross hire purchases receivables	-	10,467
Unearned interest	-	(538)
Hire purchases receivables	-	9,929
25.4 Movement in allowance for impairment		
Balance at the beginning the year	301,995	374,258
Bad debt written off during the year	(12,424)	(59,690)
Charge/(reverse) to the statement of comprehensive income	(39,171)	(12,573)
Balance at the end the year	250,400	301,995
25.4.1 Movement in individual impairment		
Balance at the beginning of the year	187,639	278,190
Bad debt written off during the year	(12,424)	(59,690)
Charge/(reverse) to the statement of comprehensive income	(11,300)	(30,861)
Balance at the end of the year	163,915	187,639
25.4.2 Movement in collective impairment		
Balance at the beginning of the year	114,356	96,068
Bad debt written off during the year	-	-
Charge/(reverse) to the statement of comprehensive income	(27,871)	18,288
Balance at the end of the year	86,485	114,356
25.5 Sector wise analysis of hire purchases receivables		
Agriculture	217,479	277,878
Industrial	415,752	519,444
Tourism	96,313	101,228
Trading	1,478,146	1,650,464
Construction	111,398	67,171
Services	4,178,903	4,325,421
Others	1,698,275	1,895,436
Total	8,196,266	8,837,042

26. Other financial assets

Accounting Policy

Insurance receivables

Premium receivables are recognised when due and measured on initial recognition at the fair value of the consideration received or receivable. The carrying value of premium receivables is reviewed for impairment whenever or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the statement of comprehensive income.

Operating lease receivables

All leases other than finance leases are classified as operating leases. When acting as lessor, the Company includes the assets subject to operating leases in 'property, plant and equipment' and accounts for them accordingly. Impairment losses are recognised to the extent that residual values are not fully recoverable and the carrying value of the assets is thereby impaired.

Rental receivable under operating leases are accounted for on a straight line basis over the periods of the leases to reduce the asset to its estimated residual value and are included in 'other operating income'. Estimated residual values are based on assumptions for used vehicle prices at lease termination and the number of vehicles that are expected to be returned.

As at 31st March	2017 Rs.'000	2016 Rs.'000
Insurance receivables	140,101	96,890
Operating leases receivables	623	332
Receivable for investment made with a primary dealer (Note 26.1)	276,178	-
Other receivables	28,884	13,218
Total	445,786	110,440
26.1 Receivable for investment made with a primary dealer		
Total receivable	693,496	-
Less: Allowance for impairment	(346,744)	-
Adjustment for effective interest rate	(70,574)	-
Total receivable at amortised cost	276,178	-

The investment made in "Repurchase Agreements" with a primary dealer appointed by the Central Bank of Sri Lanka for the purpose of complying with the "Liquid Assets Direction No.4 of 2013 issued by the Central Bank of Sri Lanka" has been reclassified from financial assets – available for sale category to loans and receivables which is included under other financial assets due to change of characteristic embedded with aforesaid investments subsequently as "ability to hold for the foreseeable future". An impairment provision of 50% for the total carrying value as at 31st March, 2017 amounting to Rs.346 Mn has been made in the financial statements as per the letter dated 12th September 2017 from the Central Bank of Sri Lanka and a 6 year repayment period was adopted to arrive at the amortised cost of the balance Rs.346 Mn as at reporting date as per the discussions had with and undertaking given by the Central Bank of Sri Lanka to pay the balance 50% as per their said letter dated 12th September, 2017 Ref:24/03/015/0014/008. The resultant adjustment of Rs.70Mn for amortised cost was charged as an interest expense to the current year.

27. Inventories

Accounting Policy

Inventory consists of spare-parts, lubricants, stationery and others. Inventories are valued at the lower of cost and estimated net realisable value, after making due allowance for obsolete and slow moving items, using weighted average cost formula. The cost of inventory is determined at actual cost.

As at 31st March	2017 Rs.'000	2016 Rs.'000
Spare-parts	4,105	4,378
Lubricant and others	1,669	2,124
Vehicle stocks	-	9,965
Stationery	2,108	-
Total	7,882	16,467

Notes to the Financial Statements

28. Other assets

Accounting Policy

Other assets mainly comprises deposits, prepayments, other advance payments, VAT receivable and sundry receivables carried at historical cost.

As at 31st March	2017 Rs.'000	2016 Rs.'000
Other receivables	20,671	11,901
Deposits and prepayments	52,077	51,529
Unamortised staff cost	8,984	8,984
Total	81,732	72,414

29. Investment in associates

Accounting Policy

Investments in associates is accounted by using the equity method in terms of the Sri Lanka Accounting Standard – LKAS 28 on "Investments in Associates". An associate is an entity in which the Company has significant influence. Significant influence is presumed to exist when the Company holds between 20% and 50% of the voting power of another entity.

Under the equity method, the investment is initially recognised at cost. The carrying amount of the investment is adjusted to recognise changes in the Company's share of net assets of associate since acquisition date.

Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The statement of comprehensive income reflects the Company's share of results of operations of the associate. When there has been a change recognised directly in the equity of the associate, the Company recognises its share of any changes, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the Company and the associate are eliminated to the extent of the interest in the associate.

The Company's share of the profit or loss of an associate is shown on the face of the statement of comprehensive income and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate.

The financial statements of the associate are prepared for the same reporting period as the Company. When necessary, adjustments are made to bring the accounting policies in line with those of the Company.

After application of the equity method, the Company determines whether it is necessary to recognise an impairment loss on its investment in its associate. The Company determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Company calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in 'share of losses of an associate' in the statement of comprehensive income.

Upon loss of significant influence over the associate, the Company measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retaining investment and proceeds from disposal is recognised in the statement of comprehensive income.

Company has a 26.12% (2016-26.12%) holding in Nuwara Eliya Hotels Company PLC which is a quoted public company and involved in the business of the hoteliering.

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Investment in associates - quoted (29.1)	995,977	927,318
Total	995,977	927,318

29.1 Investment in associates - quoted

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Nuwara Eliya Hotels Company PLC		
Carrying value at the beginning of the year	927,318	794,381
Add: Share of associates profit before tax	104,194	91,675
Share of associates tax expenses	(15,982)	(17,272)
Less : Dividend received from associates	(14,370)	(14,239)
Current year retained profit	73,842	60,164
Share of other comprehensive income	(5,183)	72,773
Carrying value at the end of the year	995,977	927,318

Summary of associate's statement of financial position

	As per audited financial statements	As per audited financial statements
As at 31st March	**2017**	**2016**
	Rs.'000	**Rs.'000**
Current assets	991,988	794,949
Non-current assets	3,107,602	3,031,602
Current liabilities	(183,718)	(177,143)
Non-current liabilities	(102,789)	(99,187)
Net assets	3,813,083	3,550,221
Holding percentage of the Company	26.12%	26.12%
Share of net assets of the Company	995,977	927,318
Market value per share (Rs.)	1,449.70	1,374.90
Total market value of the investment (Rs.'000)	758,889	719,733

The Board of Directors is in the view of temporary decline of the market value will be recovered immediately after the reporting date and this investment will be held for considering strategic advantage in future and measured the investment in associates at equity method as per LKAS 28.

As at 31st March	**2017**	**2016**
	Rs.'000	**Rs.'000**
Summary of associate's revenue and profit before tax		
Revenue	1,114,871	1,042,749
Profit before tax	398,905	350,971
Share of associate's profit before tax	104,194	91,675

30. Investment property

Accounting Policy

Recognition and measurement

Investment property 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, use in the production or supply of goods or services or for administrative purposes.

Investment property is accounted for under cost model in the financial statements. Accordingly, after initial recognition, the property is carried at its cost, less accumulated depreciation and impairment losses.

Depreciation

Depreciation is provided on a straight line basis over the estimated useful life of the class of asset from the date of purchase upto the date of disposal. Estimated useful life of the buildings classified as investment property is 40 to 75 years.

De-recognition

Investment properties are de-recognised when they are disposed of, or permanently withdrawn from use since no future economic benefits are expected. Transfers are made to and from investment property only when there is a change in use.

Notes to the Financial Statements

As at 31st March	2017 Rs.'000	2016 Rs.'000
Cost		
Balance at the beginning of the year	452,334	200,434
Additions during the year	-	280,000
Disposals during the year	(289,000)	(28,100)
Balance at the end of the year	163,334	452,334
Less : Accumulated depreciation		
Balance at the beginning of the year	4,100	1,665
Charge for the year	2,795	2,435
On disposals during the year	(1,901)	-
Balance at the end of the year	4,994	4,100
Carrying value	158,340	448,234

The Company earned rental income from the property situated at No 75A-23/2, Galle Road, Colombo 03 for which the details are given below:

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Rental income derived from investment properties	5,699	8,642
Direct operating expenses incurred generating rental income	(669)	(796)
Profit arising from investment properties	5,030	7,846

The Company has no restrictions on the realisability of its investment properties and no contractual obligations to purchase, construct or develop investment properties or for repairs, maintenance and enhancements.

30.1 Information on the investment property of the Company

As at 31st March Location	Extent (Perches)	Building (Square Feet)	2017 Cost Rs. '000	2017 Fair value Rs. '000	2016 Cost Rs. '000	2016 Fair value Rs. '000
Nilaweli						
Nilaweli Village, Pulmoddai Road, Trincomalee.	438		59,000	65,700	59,000	65,700
Kurunegala						
Sapirimini Jeewa Pohora, Thaththiripitiya, Welipennegahamulla.	80		2,500	3,000	2,500	3,000
Peliyagoda						
151/3A, Negombo Road, Peliyagoda.	5		5,000	5,500	5,000	5,500
Nugegoda						
61,Raththanapitiya Road, Gangodawila.	10.20		12,000	12,750	12,000	12,750
Homagama						
Ketakelagaha, Kuruduwatta, Henpita.	10		-	-	1,400	1,500
Ganemulla						
Karukkuwa Group Galahitiyawa.	60		-	-	2,400	2,400
Pannipitiya						
1222, Hokandara Road, Pannipitiya.	79.22		1,600	1,800	1,600	1,800
Kesbewa						
H.A.C. Alwis - 165/84, School Lane, Bokundara -Kesbewa.	21.80		-	-	5,200	5,830
Kollupitiya						
No 75A-23/2, Galle Road, Colombo 03.	-	2,636	83,234	89,900	83,234	89,900
Rathmalana						
No. 140/4, Temple Road, Rathmalana.	12.6		-	-	15,000	15,000
Colombo 02						
S.S.Tower, 92 Glennie Street, Colombo 02.	19		-	-	265,000	265,000
Total			163,334	178,650	452,334	468,380

The fair value of the investment properties as at 31st March, 2017 was based on market valuations carried out in the year 2014/2015 by a professionally qualified independent valuer Mr. P. T. T. Mohideen, Chartered Valuation Surveyor, Bsc (Hons) Estate Management and Valuation, Executive Diploma in Business Administration, FIV (Sri Lanka) and member of the Royal Institute of Chartered Surveyors - England and Directors are of the view that there is no material change in the fair values as at 31.03.2017 as per their judgement.

31. Property, plant and equipment

Accounting Policy

The Company applies the requirements of the Sri Lanka Accounting Standard - LKAS 16 on 'Property, Plant and Equipment' in accounting for its owned assets which are held for and use in the provision of services, for rental to others or for administrative purposes and are expected to be used for more than one year.

Basis of recognition

Property, plant and equipment are recognised if it is probable that future economic benefits associated with the asset will flow to the Company and cost of the asset can be reliably measured.

Basis of measurement

An item of property, plant and equipment that qualifies for recognition as an asset is initially measured at its cost. Cost includes expenditure that is directly attributable to the acquisition of the asset and subsequent costs (excluding the costs of day-to-day servicing). The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use and the costs of dismantling and removing the items and restoring the site on which they are located and capitalised borrowing costs. Purchased software which is integral to the functionality of the related equipment is capitalised as part of computer equipment. When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

Notes to the Financial Statements

Accounting Policy

Cost model

The Company applies the cost model to all property, plant and equipment except freehold land and buildings and records at cost of purchase together with any incidental expenses thereon, less accumulated depreciation and any accumulated impairment losses.

Revaluation model

The Company applies the revaluation model for the entire class of freehold land and buildings for measurement after initial recognition. Such properties are carried at revalued amounts, being their fair value at the date of revaluation, less any subsequent accumulated depreciation on buildings and any accumulated impairment losses charged subsequent to the date of valuation. Freehold land and buildings of the Company are revalued every three to five years or more frequently if the fair values are substantially different from their carrying amounts to ensure that the carrying amounts do not differ from the fair values at the reporting date.

On revaluation of an asset, any increase in the carrying amount is recognised in other comprehensive income and presented in revaluation reserve in equity or used to reverse a previous loss on revaluation of the same asset, which was charged to the statement of comprehensive income. In this circumstance, the increase is recognised as income only to the extent of the previous write down in value. Any decrease in the carrying amount is recognised as an expense in the statement of comprehensive income or charged in other comprehensive income and presented in revaluation reserve in equity only to the extent of any credit balance existing in the revaluation reserve in respect of that asset. Any balance remaining in the revaluation reserve in respect of an asset, is transferred directly to retained earnings on retirement or disposal of the asset.

The Company has revalued all its freehold land and building as at 31st March, 2015.

Subsequent cost

These are costs that are recognised in the carrying amount of an asset if it is probable that the future economic benefits embodied within that part will flow to the Company and it can be reliably measured. The costs of the day-to-day servicing of property and equipment are recognised in the statement of comprehensive income as incurred.

Restoration cost

Expenditure incurred on replacement, repairs or maintenance of property, plant and equipment in order to restore or maintain the future economic benefits expected from the originally assessed standard of performance is recognised as an expense when incurred.

Derecognition

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use. Any gain or loss arising on derecognising of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset), is recognised in 'other income/ expenses' in the statement of comprehensive income in the year the asset is derecognised.

When replacement costs are recognised in the carrying amount of an item of property, plant and equipment, the remaining carrying amount of the replaced part is derecognised as required by Sri Lanka Accounting Standard - LKAS 16 on 'Property, Plant and Equipment'.

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.

Assets on operating leases

Assets leased to customers under agreements in which we retain substantially all the risks and rewards associated with ownership and legal title are classified as operating leases. Such assets are recognised as property, plant and equipment in the statement of financial position.

31.1 Carrying value of property, plant and equipment

	At valuation		At cost							
	Land	Buildings	Motor vehicles	Plant and machinery	Computer hardware	Office equipment	Furniture, fixtures and fittings	Motor vehicle on operating leases	Capital work-in-progress	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
2017 - Current year										
Cost/ valuation										
Balance as at 01.04.2016	856,350	587,750	284,526	17,790	89,264	54,294	59,931	25,600	23,918	1,999,423
Additions during the year	-	921	-	10,509	34,385	12,504	9,488	4,150	13,420	85,377
Disposals during the year	-	-	(40,591)	(210)	(785)	(2,007)	(432)	-	-	(44,025)
Derecognition	-	-	-	(23)	-	(2,342)	(765)	-	-	(3,130)
Cost/ valuation as at 31.03.2017	856,350	588,671	243,935	28,066	122,864	62,449	68,222	29,750	37,338	2,037,645
Accumulated depreciation										
Balance as at 01.04.2016	-	11,755	82,659	6,953	53,468	18,169	19,649	2,831	-	195,484
Charge for the year	-	11,755	14,046	4,060	16,805	5,712	6,317	4,442	-	63,137
On disposals during the year	-	-	(6,566)	(55)	(414)	(1,017)	(91)	-	-	(8,143)
Derecognition	-	-	-	(22)	-	(2,342)	(765)	-	-	(3,129)
Accumulated depreciations as at 31.03.2017	-	23,510	90,139	10,936	69,859	20,522	25,110	7,273	-	247,349
Net book value as at 31.03.2017	856,350	565,161	153,796	17,130	53,005	41,927	43,112	22,477	37,338	1,790,296
2016 - Previous year										
Cost/valuation										
Balance as at 01.04.2015	856,350	587,750	311,285	34,248	88,423	58,820	64,516	9,500	-	2,010,892
Additions during the year	-	-	15,769	5,133	23,255	12,330	10,437	16,100	23,918	106,942
On disposals during the year	-	-	(42,528)	-	-	(83)	-	-	-	(42,611)
Derecognition	-	-	-	(21,591)	(22,414)	(16,773)	(15,022)	-	-	(75,800)
Cost/ valuation as at 31.03.2016	856,350	587,750	284,526	17,790	89,264	54,294	59,931	25,600	23,918	1,999,423
Accumulated depreciation										
Balance as at 01.04.2015	-	-	105,614	25,726	62,928	30,202	29,370	927	-	254,767
Charge for the year	-	11,755	7,141	2,818	12,954	4,769	5,301	1,904	-	46,642
On disposals during the year	-	-	(30,096)	-	-	(29)	-	-	-	(30,125)
Derecognition	-	-	-	(21,591)	(22,414)	(16,773)	(15,022)	-	-	(75,800)
Accumulated depreciations at 31.03.2016	-	11,755	82,659	6,953	53,468	18,169	19,649	2,831	-	195,484
Net book value as at 31.03.2016	856,350	575,995	201,867	10,837	35,796	36,125	40,282	22,769	23,918	1,803,939

31.2 Revaluation of property, plant and equipment

The land and buildings were revalued during the financial year 2014/2015 by a professionally qualified independent valuer, Mr. P.P.T. Mohideen, Chartered Valuation Surveyor, B.Sc. (Hons) Estate Management & Valuation, Executive Diploma in Business Administration, FIV (Sri Lanka) and Member of the Royal Institution of Chartered Surveyors – England. The results of such revaluation was incorporated in these financial statements from its effective date which was 31st March, 2015. Such assets were valued on an open market value for an existing use basis. The surplus arising from the revaluation was transferred to revaluation reserve.

Notes to the Financial Statements

31.3 Information on the freehold land and building of the Company

As required by rule No. 7.6 (VIII) of the continuing listing requirements of the Colombo Stock Exchange.

	Extent (Perches)	Buildings (Square feet)	Revalued amount of buildings	Revalued amount of land	Net book value as at 31.03.2017	As a % of total NBV as at 31.03.2017	Net book value as at 31.03.2016	As a % of total NBV as at 31.03.2016
Location	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	
At revaluation								
Kollupitiya No. 236, Galle Road, Colombo 03.	32.56	46,777	314,400	309,000	623,400	43.85	629,950	43.98
Maharagama No. 176, Lake Road, Maharagama.	168.74	22,900	18,240	169,000	187,240	13.17	187,620	13.10
Maharagama No. 16, Batadombagahawatta Lane, Godigamuwa, Maharagama.	104.00	9,355	10,080	67,500	77,580	5.46	77,790	5.43
Kohuwala No. 28, Sunethra Devi Road, Kohuwala.	88.00	27,543	66,873	220,000	286,873	20.18	287,326	20.06
Kohuwala No. 30/8, Sunethra Devi Road, Kohuwala.	17.80	1,700	4,656	22,250	26,906	1.89	27,003	1.89
Borella No. 219, Dr. N.M. Perera Mw, Colombo 08.	9.46	6,264	40,032	38,600	78,632	5.53	79,466	5.55
Negombo No. 26A, Colombo Road, Negombo.	13.87	-	-	20,000	20,000	1.41	20,000	1.40
Kollupitiya No. 75-17/4, Galle Road, Colombo 03.	-	1,210	27,840	-	27,840	1.96	28,420	1.98
Kollupitiya No. 89-28/4 & 89-28/5, Galle Road, Colombo 03.	-	3,583	83,040	-	83,040	5.84	84,770	5.92
Negombo 814/24, Colombo Road, Negombo.	17.20	-	-	10,000	10,000	0.70	10,000	0.70
Total	-	-	565,161	856,350	1,421,511	100	1,432,345	100

31.4 Revaluation

Freehold land and building of the Company were revalued by a professionally qualified independent valuer (Mr. P.P.T Mohideen) as at 31st March, 2015.

	Method of valuation and significant unobservable inputs	Range of estimates for unobservable inputs	NBV before revaluation As at 31st March, 2015		Revalued amount of		Revaluation gain/ (loss) recognised on	
Location			**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**
Kollupitiya - No. 236, Galle Road, Colombo 03.	Open market basis		285,854	227,900	327,500	309,000	41,646	81,100
	Price per perch of land (Rs.)	9,500,000.00						
	Price per square foot for building (Rs.)	7,001.30						
Maharagama - No. 176, Lake Road, Maharagama.	Open market basis		20,001	135,000	19,000	169,000	(1,001)	34,000
	Price per perch of land (Rs.)	1,000,000.00						
	Price per square foot for building (Rs.)	829.69						
Maharagama - No. 16, Batadombagahawatta Lane, Godigamuwa, Maharagama.	Open market basis		7,990	52,000	10,500	67,500	2,510	15,500
	Price per perch of land (Rs.)	650,000.00						
	Price per square foot for building (Rs.)	1,122.39						
Kohuwala - No. 28, Sunethra Devi Road, Kohuwala.	Open market basis		57,121	176,000	68,700	220,000	11,579	44,000
	Price per perch of land (Rs.)	2,500,000.00						
	Price per square foot for building (Rs.)	2,494.28						
Kohuwala - No. 30/8, Sunethra Devi Road, Kohuwala.	Open market basis		3,954	17,800	4,850	22,250	896	4,450
	Price per perch of land (Rs.)	1,250,000.00						
	Price per square foot for building (Rs.)	2,852.94						
Borella - No. 219, Dr. N. M. Perera Mw, Colombo 08.	Open market basis		52,785	30,000	41,700	38,600	(11,085)	8,600
	Price per perch of land (Rs.)	4,500,000.00						
	Price per square foot for building (Rs.)	7,487.23						
Negombo - No. 26A, Colombo Road, Negombo.	Open market basis		-	17,000	-	20,000	-	3,000
	Price per perch of land (Rs.)	1,450,000.00						
Kollupitiya - No. 75-17/4, Galle Road, Colombo 03.	Investment method		22,372	-	29,000	-	6,628	-
	Gross annual rentals (Rs.)	1,680,000.00						
	Years purchase(present value of 1 unit per period)	23 Y.P						
Kollupitiya - No. 89-28/4 & 89-28/5, Galle Road, Colombo 03.	Investment method		66,740	-	86,500	-	19,760	-
	Gross annual rentals (Rs.)	4,920,000.00						
	Years purchase(present value of 1 unit per period)	23.5 Y.P						
Negombo - No. 814/24, Colombo Road, Negombo.	Open market basis		-	10,027	-	10,000	-	(27)
	Price per perch of land (Rs.)	585,000.00						
Total			516,817	665,727	587,750	856,350	70,933	190,623

Notes to the Financial Statements

Narrative descriptions on the sensitivity of fair value measurement to changes in significant unobservable inputs are tabled below:

Valuation technique	Significant unobservable valuation inputs	Sensitivity of the fair value measurement to inputs
Market comparable method In determining the fair value of the property being revalued, this method considers the selling price of a similar property within a reasonably recent period of time. This involves evaluating recent active market prices of similar assets, making appropriate adjustments for differences in size, nature, location and condition of the specific property.	• Price per perch for land • Price per square foot for building	Estimated fair value would increase (decrease) if; • Price per perch would be higher (lower) • Price per square foot would be higher (lower)
Investment method This method involves the capitalisation of the expected rental income over a specific period of time which is derived from the real estate market.	• Gross annual rentals • Years purchase	Estimated fair value would increase (decrease) if; • Gross annual rentals would be higher (lower) • Years purchase would be higher (lower)

31.5 The carrying amounts of revalued assets, that would have been included in the financial statements, had the assets been carried at cost are as follows:

	2017			2016		
As at 31st March	**Cost**	**Cumulative depreciation**	**Net carrying amount**	**Cost**	**Cumulative depreciation**	**Net carrying amount**
	Rs.'000	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**	**Rs.'000**
Class of asset						
Freehold land	160,521	-	160,521	160,521	-	160,521
Freehold buildings	252,923	79,344	173,579	252,923	74,286	178,637
	413,444	79,344	334,100	413,444	74,286	339,158

31.6 During the financial year, the Company acquired property, plant and equipment to the aggregate value of Rs.71,958,192/- (2016 - Rs.83,022,926/-).

Cash payments amounting to Rs.71,958,192/- (2016 - Rs.83,022,926/-) were made during the year for purchase of property, plant and equipment.

31.7 Property, plant and equipments include assets under operating leases, where the Company is a lessor. The net carrying amount of those assets as at 31st March 2017 was Rs. 22,478,548/- (2016 - Rs. 22,770,360/-), on which the accumulated depreciation as at 31st March, 2017 was Rs. 7,271,451/- (2016-Rs. 2,829,640/-) .

Summary of future operating lease receivable is as follows:

	Within one year	1-5 years	Over 5 years	Total
	Rs.'000	**Rs.'000**	**Rs.'000**	**Rs.'000**
As at 31st March, 2017				
Future operating lease receivable	9,166	19,244	-	28,411
As at 31st March, 2016				
Future operating lease receivable	7,958	23,691	-	31,649

31.8 Temporarily idle property, plant and equipment

There were no temporary idle property, plant and equipment or any asset retired from active use and held for disposal on the date of statement of financial position.

31.9 Fully depreciated property, plant and equipment

The cost of property, plant and equipment as at reporting date includes the fully depreciated assets amounting to Rs.49,485,728/- (2016 - Rs.28,299,699/-)

31.10 Property, plant and equipment pledged as security for liabilities

There were no property, plant and equipment pledged as securities for liabilities except properties at Sri Vajiragnana Mawatha, Maharagama and No. 28, Sunethradevi Road, Kohuwala pledged as securities for overdraft facilities obtained from Sampath Bank PLC and Hatton National Bank PLC respectively for Rs.100 Mn each.

31.11 Title restriction in property, plant and equipment

There were no restrictions that existed in the title of the property, plant and equipment of the Company as at reporting date except properties at Sri Vajiragnana Mawatha, Maharagama and No.28, Sunethradevi Road, Kohuwala pledged as securities for overdraft facilities obtained from Sampath Bank PLC and Hatton National Bank PLC respectively.

31.12 Compensation from third parties for items of property, plant and equipment

There were no compensation received /receivable from third parties for items of property, plant and equipment that were impaired, lost or given up. (2016 - Rs. 2,991,900/-)

31.13 Capitalisation of borrowing cost

There were no borrowing costs that have been capitalised into the capital work-in-progress.

31.14 Capital commitments

There are no significant capital commitments which have been approved or contracted for by the Company as at 31st March, 2017.

32. Leasehold property

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Cost		
At the beginning of the year	46,354	46,354
Additions	-	-
Disposals	-	-
At the end of the year	46,354	46,354
Accumulated amortisation and impairment		
At the beginning of the year	3,746	3,278
Amortisation for the year	468	468
Disposals	-	-
Impairment	-	-
At the end of the year	4,214	3,746
Net book value as at 31st March	42,140	42,608

Notes to the Financial Statements

33. Intangible assets

Accounting Policy

Basis of recognition

An intangible asset is recognised if it is probable that future economic benefits that are attributable to the asset will flow to the entity and the cost of the asset can be measured reliably in accordance with LKAS 38 'Intangible Assets'. Accordingly, these assets are stated in the statement of financial position at cost, less accumulated amortisation and accumulated impairment losses, if any.

Subsequent expenditure

Subsequent expenditure on intangible assets is capitalised only when it increases the future economic benefits embodied in these assets. All other expenditure is charged to the statement of comprehensive income when incurred.

Useful economic lives, amortisation and impairment

The Company does not possess intangible assets with indefinite useful lives. Useful economic lives, amortisation and impairment of finite intangible assets are described below:

Intangible assets with finite lives and amortisation

Intangible assets with finite lives are amortised over the useful economic lives. The amortisation period and the amortisation method for an intangible asset with finite useful life are reviewed at least at each reporting date. Changes in the expected useful life or the expected pattern of consumption of future economic benefit embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the statement of comprehensive income as an expense.

Computer software

All computer software costs incurred, licensed for use by the Company, which are not integrally related to associated hardware, which can be clearly identified, reliably measured and it is probable that they will lead to future economic benefits, are included in the statement of financial position under the category of intangible assets and carried at cost, less accumulated amortisation and accumulated impairment losses, if any.

Derecognition of intangible assets

Intangible assets are derecognised on disposal or when no future economic benefits are expected from its use. Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the statement of comprehensive income.

As at 31st March	2017 Rs.'000	2016 Rs.'000
Cost		
At the beginning of the year	28,801	19,310
Additions	2,977	9,491
Derecognition	(473)	-
At the end of the year	31,305	28,801
Accumulated amortisation and impairment		
At the beginning of the year	16,415	15,966
Amortisation for the year	2,786	449
Derecognition	(473)	-
At the end of the year	18,728	16,415
Net book value as at 31st March	12,577	12,386

34. Deposits due to customers

These include fixed deposits, savings deposits and certificate of deposits. Subsequent to initial recognition deposits are measured at their amortised cost using the Effective Interest Rate method (EIR). Interest paid/payable on these deposits is recognised in the statement of comprehensive income.

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Fixed deposits (Note 34.1)	16,964,298	15,726,830
Certificate of deposits (Note 34.2)	16,482	24,921
Savings deposits	36,894	63,839
Total	17,017,674	15,815,590
34.1 Analysis of fixed deposits by maturity date		
1 to 90 days	5,529,427	4,472,980
91 to 365 days	7,555,160	7,308,820
More than 365 days	3,879,711	3,945,030
Total	16,964,298	15,726,830
34.2 Analysis of certificate of deposits by maturity date		
1 to 90 days	8,038	12,785
91 to 365 days	8,444	12,136
More than 365 days	-	-
Total	16,482	24,921

35. Debts instruments issued and other borrowings

Accounting Policy

These represent the funds borrowed by the Company for long term funding requirements. Subsequent to initial recognition debt securities issued are measured at their amortised cost using the EIR method except where the Company designates debt securities issued at fair value through profit or loss. Interest paid or payable is recognised in the statement of comprehensive income.

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Money market borrowings	200,000	200,000
Short term borrowings (Note 35.1)	3,114,632	2,308,330
Long term borrowings (Note 35.2)	6,340,975	5,611,450
Debt instruments (Note 35.3)	200,000	200,000
Interest payable	310,230	207,389
Total	10,165,837	8,527,169

Notes to the Financial Statements

35.1 Short term borrowings

As at 31st March	Terms of repayment			2017	2016
	Interest Rate	Period	Payment terms	Rs.'000	Rs.'000
National Development Bank PLC	14.50%	1 month	At maturity	500,000	750,000
National Development Bank PLC	12.65%	Quarterly	At maturity	125,000	-
National Development Bank PLC	14.50%	1 month	At maturity	150,000	-
National Development Bank PLC	14.10%	1 month	At maturity	500,000	-
Bank of Ceylon	13.99%	1 year	At maturity	441,143	-
Capital Alliance Ltd	9.50%	Overnight	At maturity	98,489	-
Sampath Bank PLC	15.00%	1 month	At maturity	500,000	-
Hatton National Bank PLC	14.00%	1 year	At maturity	750,000	-
Cargills Bank	12.50%	3 months	At maturity	50,000	-
Commercial Bank of Ceylon PLC	9%	1 year	At maturity	-	458,330
Nations Trust Bank PLC	10.36%	1 month	At maturity	-	200,000
Hongkong & Shanghai Bank Corporations Ltd	9.50%	1 month	At maturity	-	100,000
Hongkong & Shanghai Bank Corporations Ltd	7.80%	1 month	At maturity	-	400,000
Seylan Bank PLC	8.75%	1 week	At maturity	-	400,000
Total				3,114,632	2,308,330

35.2 Long term borrowings

As at 31st March	Terms of repayment			2017	2016
	Interest Rate	Period	Payment terms	Rs.'000	Rs.'000
Central Bank of Sri Lanka (Refinanced borrowings)	6%	8 years	Semi annual instalment	-	7,813
Securitised borrowings	8.47% -13.66%	3 to 4 years	Variable monthly instalment	2,190,245	2,263,093
Hatton National Bank PLC	8.50%	4 years	Fixed monthly instalment	207,960	333,120
Hatton National Bank PLC	9.50%	4 years	Fixed monthly instalment	687,501	937,500
Commercial Bank of Ceylon PLC	AWPLR+1.5%	4 years	Fixed monthly instalment	17,000	143,000
Commercial Bank of Ceylon PLC	9.5%	4 years	Fixed monthly instalment	174,500	300,500
Commercial Bank of Ceylon PLC	8.5%	4 years	Fixed monthly instalment	458,160	708,240
Commercial Bank of Ceylon PLC	10.50%	3 years	Fixed monthly instalment	319,300	486,100
Commercial Bank of Ceylon PLC	11.75%	15 months	Fixed monthly instalment	266,300	-
Commercial Bank of Ceylon PLC	15.00%	4 years	Fixed monthly instalment	1,000,000	-
Seylan Bank PLC	8.50%	2 years	Fixed monthly instalment	104,167	354,167
Seylan Bank PLC	14.25%	2 years	Fixed monthly instalment	708,333	-
Cargills Bank	12%-AWPLR+1	5 years	Fixed monthly instalment	207,509	-
Bank of Ceylon	8.5%	15 months	Fixed monthly instalment	-	77,917
Total				6,340,975	5,611,450

Maturity analysis of borrowings and assets pledged details are given in the note 52 and 49 to the financial statements respectively.

35.3 Debt instruments

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Unsecured redeemable debentures (Note 35.3.1)	200,000	200,000
Total	200,000	200,000

35.3.1 Unsecured redeemable debentures

No of debentures	2,000,000
Face value (Rs.)	200,000,000
Category	Fixed rate debenture 2014/2018
Colombo stock exchange listing	Listed
Interest payable frequency	Annually
Allotment date	11.07.2014
Maturity date	11.07.2018
Effective annual yield	10.50%

36. Other financial liabilities

As at 31st March	2017 Rs.'000	2016 Rs.'000
Vendor payable	575,337	892,270
Insurance payable	137,744	87,731
Other payable	63,738	72,326
	776,819	1,052,327

37. Deferred tax liabilities

Accounting Policy

Deferred tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except;

» Where the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

» In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax assets and unused tax losses can be utilised: except

» Where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

» In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the reporting date.

The deferred tax relating to items recognised directly in equity are also recognised in equity, and not in the statement of comprehensive income.

Notes to the Financial Statements

As at 31st March	2017		2016	
	Temporary difference	Tax effect	Temporary difference	Tax effect
	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Summary of net deferred tax liability				
Balance at the beginning of the year	1,225,920	343,259	791,438	221,601
Amount originating/(reversing) during the year	56,312	15,767	380,033	106,410
Deferred tax effect on revaluation surplus on PPE	(2,246)	(629)	57,463	16,092
Deferred tax effect on actuarial gain	10,094	2,826	(3,014)	(844)
Balance at the end of the year	1,290,080	361,223	1,225,920	343,259
Deferred tax asset				
Retirement benefit obligation	172,957	48,428	146,236	40,946
Tax loss from leasing activities	93,635	26,218	165,415	46,316
Unclaimed impairment provision	399,208	111,778	41,409	11,594
	665,800	186,424	353,060	98,856
Deferred tax liability				
Accelerated depreciation for tax purpose - leased assets	(1,366,038)	(382,491)	(1,022,151)	(286,203)
Accelerated depreciation for tax purpose - owned assets	(213,279)	(59,718)	(178,019)	(49,845)
Deferred tax effect on revaluation surplus	(376,563)	(105,438)	(378,810)	(106,067)
	(1,955,880)	(547,647)	(1,578,980)	(442,115)
Net temporary difference and deferred assets/(tax liability)	(1,290,080)	(361,223)	(1,225,920)	(343,259)

38. Retirement benefit obligations

Accounting Policy

The Company measures the present value of the promised retirement benefits for gratuity, which is a defined benefit plan with the advice of an independent professional actuary using the Projected Unit Credit (PUC) method as required by Sri Lanka Accounting Standard LKAS No. 19 - on 'Employees Benefits'. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflow using interest rates that apply to the currency in which the benefits will be paid.

The Company policy is to perform actuarial valuation in every year.

Provision has been made for retirement gratuities from the first year of service for all employees in conformity with the LKAS 19 on 'Employees Benefits'.

However, under the Payment of Gratuity Act No. 12 of 1983, the liability to an employee arises only on completion of 5 years of continued service.

As at 31st March	2017	2016
	Rs.'000	Rs.'000
38.1 Provision for retirement benefit obligations		
Balance at the beginning of the year	146,235	120,118
Expenses recognised during the year (Note 38.2)	29,512	34,734
Payments made during the year	(3,975)	(8,617)
Balance at the end of the year	171,772	146,235
38.2 Expenses recognised in the statement of comprehensive income		
Interest cost - statement of comprehensive income	14,624	12,012
Current service cost - statement of comprehensive income	13,703	11,444
	28,327	23,456
Actuarial (gain) / loss - other comprehensive income	1,185	11,278
	29,512	34,734

Actuarial valuation of the gratuity liability was carried out as at 31st March, 2017 by Messers Actuarial & Management Consultants (Pvt) Ltd, a firm of professional actuaries. The valuation method used by the actuaries to value the fund is the 'Projected Unit Credit method' (PCU), the method recommended by the Sri Lanka Accounting Standard (LKAS 19) on 'Employee Benefits'.

38.3 Actuarial assumptions - demographic

Mortality
In service - A 67/70 Mortality table issued by the Institute of Actuaries, London.

Withdrawal
The withdrawal rate at an age represents the probability of an employee leaving within one year of that age due to reasons other than death, ill health and normal retirement. Withdrawal rate of 13% used in this valuation have been determined based on the staff turnover statistics of the Company. (Previous year 11%).

Disability
The disability rate at an age represents the probability of an employee leaving within one year of that age due to ill health/disability. Assumptions similar to those used in other comparable plans for disability were used as the data required to do a “scheme specific” study was not available.

Normal retirement age
55 to 60 years, The employees who are aged over the specified retirement age have been assumed to retire on their respective next birthdays. (Previous year 55 years to 60 years).

Actuarial assumptions - financial

Rate of discount
In the absence of a deep market in long term bonds in Sri Lanka ,a long term rate of discount of 12.21% has been used having given weightage to the anticipated long term rate of inflation. (Previous year 10%).

Salary increases
A 10% p.a salary increment rate has been used in respect of the active employees. (Previous year 8%).

38.4 Sensitivity analysis

In order to show the significance of the salary escalation rate and discount rate used in the actuarial valuation as at 31st March, 2017, sensitivity analysis has been carried out as follows:

Discount rate	Salary escalation rate	Present value of defined benefit obligation
		Rs.
1% Increase	As the rate above	163,594,767
1% Decrease	As the rate above	180,804,125
As the rate above	1% Increase	180,192,219
As the rate above	1% Decrease	164,023,108

39. Stated capital

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Value		
Ordinary shares	36,000	36,000
	36,000	36,000

Notes to the Financial Statements

As at 31st March	2017 (Nos '000)	2016 (Nos '000)
Number of shares in issue		
Ordinary shares	3,006	3,006
	3,006	3,006

40. Capital reserve - revaluation reserve

As at 31st March	2017 Rs.'000	2016 Rs.'000
Balance at the beginning of the year	1,539,615	1,482,934
Increase during the year due to revaluation	(5,183)	72,773
Deferred tax effect	629	(16,092)
Balance at the end of the year	1,535,061	1,539,615

The revaluation reserve relates to revaluation of land and buildings of the company and its associates company and represents the increase in the fair value of the land and buildings at the date of revaluation.

41. Statutory reserve fund

As at 31st March	2017 Rs.'000	2016 Rs.'000
Balance at the beginning of the year	631,400	581,400
Transfers during the year	30,000	50,000
Balance at the end of the year	661,400	631,400

Statutory reserve fund which is a capital reserve, was created in accordance with the Finance Companies Direction No. 1 of 2003 issued by the Central Bank of Sri Lanka.

42. General reserve

As at 31st March	2017 Rs.'000	2016 Rs.'000
Balance at the beginning of the year	4,086,430	3,886,430
Transfers during the year	-	200,000
Balance at the end of the year	4,086,430	4,086,430

The company maintains the general reserve to retain funds for future expansion. During the year company has not allocated funds to general reserve.

43. Retained earnings

As at 31st March	2017 Rs.'000	2016 Rs.'000
Balance at the beginning of the year	1,123,727	900,184
Total comprehensive income		
Profit for the year	202,014	505,019
Other comprehensive income	(4,011)	(10,434)
Transfer to general reserve	-	(200,000)
Transfer to statutory reserve	(30,000)	(50,000)
Dividend paid	-	(21,042)
Balance at the end of the year	1,291,730	1,123,727

44. Available-for-sale reserve

As at 31st March	2017 Rs.'000	2016 Rs.'000
Balance at the beginning of the year	237,060	892,817
Net gain and losses on remeasuring of AFS financial assets	19,584	(655,757)
Balance at the end of the year	256,644	237,060

The available for sale reserve comprises the cumulative net change in fair value of financial investment available for sale, until such investment are derecognised or impaired.

44.1 During the year the company has recognised an impairment in the market value of its available for sale financial assets amounting to Rs. 96.992Mn as per paragraph 61 of LKAS 39 - Financial instruments - recognition and measurement.

45. Capital commitments

There are no significant capital commitments which have been approved or contracted for by the Company as at 31st March, 2017.

46. Contingencies

46.1 Contingent liabilities

Accounting Policy

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is not probable or cannot be readily measured as defined in the Sri Lanka Accounting Standard - LKAS 37 on 'Provisions, Contingent Liabilities and Contingent Assets'.

Contingent liabilities are not recognised in the statement of financial position but are disclosed unless its occurrence is remote.

The Company does not anticipate any contingent liabilities to arise out of any contingent event as at the date of statement of financial position except as disclosed below :

a) The gratuity liability of the Company as at 31st March, 2017 is based on the actuarial valuation carried out by Ms. Actuarial & Management Consultants (Pvt) Ltd, a firm of professional actuaries. As per the actuarial valuation, the provision in respect of gratuity liabilities of the existing employees of the Company as at 31st March, 2017 is Rs. 171,772,639/-. If the Company had provided for gratuity on the basis of Gratuities Act No.12 of 1983, the liability would have been Rs. 204,531,642/-. Hence, there is a contingent liability of Rs.32,759,003/-, which would crystallize only if the Company ceases to be a going concern.

b) Few litigations filed by the customers against the Company.
Although there can be no assurance, the directors believe, based on the information currently available, that the ultimate resolution of such legal procedures would not likely to have a material adverse effect on the results of operations, financial position or liquidity. Accordingly no provision for any liability has been made in these financial statements.

46.2 Contingent assets

There are no contingent assets as at the date of statement of financial position.

47. Trust activities

The Company is not engaged in any trust activities which may have an impact on its financial results, financial position or liquidity of the Company.

48. Related party disclosure

The Company carries out transactions in the ordinary course of business on an arm's length basis at commercial rates with related parties. Except for the transactions that key management personnel (KMPs) have made under schemes uniformly applicable to all the staff at concessionary rates, transactions with the related parties listed below have been at commercial rates.

48.1 Parent and ultimate controlling party

The Company does not have an identifiable parent of its own.

Notes to the Financial Statements

48.2 Transactions with the key management personnel

Key management personnel (KMP) are those persons having authority and responsibility for directing, planning and controlling the activities of the Company directly or indirectly. The Board of Directors (including executive and non-executive) of the Company have been classified as key management personnel.

Apartment No.89-28/4 and 89-28/5, Galle Road, Colombo - 03 is being currently used by one of the key management personnel without any charges for residential purpose.

For the year ended 31st March	2017	2016
	Rs.'000	Rs.'000
Short - term employee benefits	26,135	23,447
Directors' remuneration	59,491	53,628
	85,626	77,075

48.3 Transactions involving key management personnel (KMPs) and their close family members (CFMs)

Close family members (CFM) are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity and include children, spouse or domestic partner of KMP.

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Statement of financial position		
Liabilities		
Deposits	580,640	497,272
	580,640	497,272
Statements of comprehensive income		
Interest expenses	85,852	54,012
Other transactions		
Dividend paid on shareholding	-	10,092

48.4 Transactions with the entities which are controlled by key management personnel (KMPs) and their close family members (CFMs).

48.4.1 Statement of financial position

As at 31st March	2017	2016
	Rs.'000	Rs.'000
Assets		
Loan and advances	7,755	14,331
Other receivables	1,822	326
Total	9,577	14,657
Accommodation as a % of capital funds	0.01%	0.19%
Liabilities		
Deposits	1,285,359	1,022,306
Accrued expenses	2,572	2,703
	1,287,931	1,025,009

Statements of comprehensive income

For the year ended 31st March	2017 Rs.'000	2016 Rs.'000
Interest income on loans and advances	668	1,251
Interest expenses on fixed deposits	104,789	70,238
Rent income	7,050	4,800
Other income	8,902	7,314
Security expenses	27,884	26,308

48.4.2 Transactions with the associates

Statement of financial position

As at 31st March	2017 Rs.'000	2016 Rs.'000
Assets		
Other assets	4	3
Liabilities		
Deposits	590,264	456,794
Statements of comprehensive income		
Interest expenses on fixed deposits	47,173	26,966
Rent income	1,500	1,200
Other income	2,524	1,599
Other transactions		
Dividend income	14,370	14,239

49. Assets pledged

The following assets have been pledged as security for banking and loan facilities

Name of the bank	Nature of the facility	Facility amount (Rs.)	Outstanding as at 31st March 2017 (Rs.)	Securities/ mortgages
Commercial Bank of Ceylon PLC	Overdraft	125 Mn	176,945,234	Mortgaged over investment in quoted shares by the Company.
	Money market loan	200 Mn	200,000,000	Mortgaged over hire purchase & leases receivables for Rs. 260 Million.
	Term loan	500 Mn	17,000,000	Mortgaged over hire purchase & leases receivables for Rs. 650 Million.
	Term loan	500 Mn	174,500,000	Mortgaged over hire purchase & leases receivables for Rs. 500 Million.
	Term loan	500 Mn	319,300,000	Mortgaged over hire purchase & leases receivables for Rs.500 Million.
	Term loan	1 Billion	458,160,000	Mortgaged over hire purchase & leases receivables for Rs.1.3 Billion.
	Term loan	1 Billion	266,300,000	Mortgaged over hire purchase & leases receivables for Rs.1.3 Billion.
	Term loan	1 Billion	1,000,000,000	Mortgaged over hire purchase & leases receivables for Rs.1.3 Billion.
Hatton National Bank PLC	Overdraft	400 Mn	(1,091,286,172)	Mortgaged over investment in quoted shares by the Company.
	Term loan	500 Mn	207,960,000	Mortgaged over hire purchase & leases receivables for Rs. 700 Million

Notes to the Financial Statements

Name of the bank	Nature of the facility	Facility amount (Rs.)	Outstanding as at 31st March 2017 (Rs.)	Securities/ mortgages
	Term loan	1000 Mn	687,500,500	Mortgaged over hire purchase & leases receivables for Rs. 1Billion
	Term loan	1 Billion	750,000,100	Mortgaged over hire purchase & leases receivables for Rs. 1 Billion
Sampath Bank PLC	Overdraft	100 Mn	1,513,977	Mortgaged over property at Vajiragnana Mawatha, Maharagama for Rs.100 Million.
				Promissory note for Rs.100 Million.
	Money Market	500 Mn	500,000,000	Clean
Seylan Bank PLC	Term loan	500 Mn	104,166,654	Mortgaged over hire purchase & leases receivables for Rs.2 Billion
	Term loan	1 Billion	708,333,331	
Bank of Ceylon PLC	Term loan	500 Mn	441,142,760	Mortgaged over hire purchase & leases receivables for Rs.2 Billion
Cargills Bank	Term loan	250 Mn	207,508,789	Mortgaged over hire purchase & leases receivables for Rs.500 Million
	Money Market Loan	50 Mn	50,000,000	Clean
National Development Bank PLC	Term loan	500 Mn	500,000,000	Mortgaged over hire purchase & leases receivables for Rs.2375 Mn.
		125 Mn	125,000,000	
		150 Mn	150,000,000	
		500 Mn	500,000,000	
Capital Alliance	Repo borrowings	100 Mn	98,489,358	Treasury Bonds of Rs.142 Million
Securitised borrowings	Term loan (Trust 15)	1000 Mn	566,400,000	Mortgaged over hire purchase & leases receivables for Rs. 1 Billion
	Term loan (Trust 13)	824.6 Mn	16,100,000	Mortgaged over hire purchase & leases receivables for Rs. 824.6 Million
	Term loan (Trust 14)	567.061 Mn	103,776,475	Mortgaged over hire purchase & leases receivables for Rs. 567 Million
	Term loan (Trust 16)	870 Mn	653,968,601	Mortgaged over hire purchase & leases receivables for Rs. 870 Million
	Term loan BOC (Trust 1)	1000 Mn	850,000,000	Mortgaged over hire purchase & leases receivables for Rs. 1 Billion.
			2,190,245,076	

50. Events After The Reporting Date

Accounting Policy

Events after the reporting period are those events, favourable and unfavourable, that occur between the reporting date and the date when the financial statements are authorised for issue. In this regard, all material and important events that occurred after the reporting period have been considered and appropriate disclosures are made into the financial statements where necessary.

Subsequent to the reporting date, no circumstances have arisen which would require adjustments to or disclosures in the financial statements.

51. Financial reporting by segments as per the provisions of Sri Lanka Financial Reporting Standard - SLFRS 08

Accounting Policy

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses, including revenues and incur expenses, that relate to transactions with any of the Company's other components, whose operating results are reviewed regularly by the Company management committee (being the chief operating decision-maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

As per the provisions of Sri Lanka Reporting Standard - SLFRS 8, the operating segments of the Company has been identified based on the products and services offered by the Company of which level of risk and rewards are significantly differ from one another.

The operating business are organised and managed separately according to the nature of the products and services provided with each segment representing a strategic business unit that offers different products and serves different markets. The operating segments identified by the Company are as follows:

Finance lease	This segment includes finance leasing products offered to the customers
Hire purchase	This segment includes hire purchase products offered to the customers
Loans and advances	This segment include vehicle loans, loans against property mortgages and micro finance lending
Investments	This segment includes the investments in equities and debt securities
Other	This segment includes all other business activities other than the above segments

The Company has aggregated all other business lines under "other segment" considering the risks & rewards and the materiality criteria.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. The accounting policies adopted for segment reporting are those accounting policies adopted for preparing financial statements of the Company. Inter-segment transfers are accounted at arms length basis.

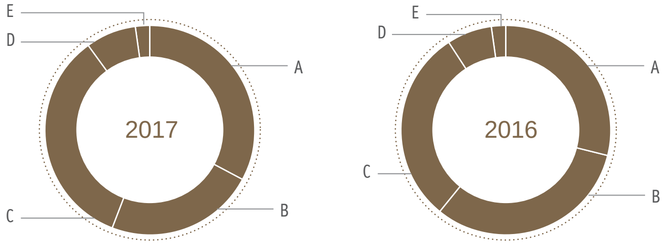
Notes to the Financial Statements

51.1 Business Segments

The following table presents the income, profit and assets and liability information on the Company business's segment for the year ended 31st March, 2017 and comparative figures for the year ended 31st March, 2016.

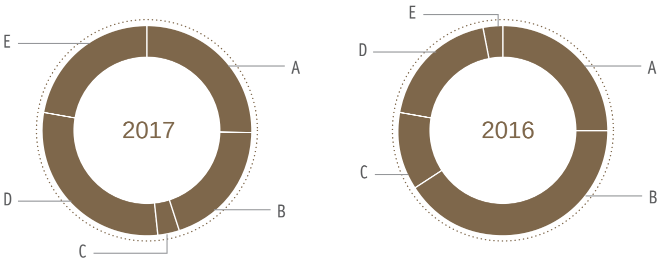
	Finance Lease		Hire Purchase	
For the year ended 31st March	**2017**	**2016**	**2017**	**2016**
	Rs. '000	**Rs. '000**	**Rs. '000**	**Rs. '000**
External operating income				
Interest income	1,873,991	1,317,611	1,262,361	1,459,426
Interest expenses	1,041,043	629,510	701,269	697,264
Net interest income/(expenses)	832,948	688,101	561,092	762,162
Fee and commission income	-	-	-	-
Capital gains	-	-	-	-
Dividends	-	-	-	-
Others	-	-	-	-
Total operating income	832,948	688,101	561,092	762,162
Impairment charge/(reversal) for loans and receivables	(25,807)	49,100	(39,171)	(12,573)
Net operating income	858,755	639,001	600,263	774,735
Personnel expenses	234,979	159,608	158,287	176,787
Commission	53,855	62,456	33,244	37,353
Depreciation and amortisation	23,970	14,998	16,147	16,612
Disallowed VAT on expenses	9,608	3,606	6,472	3,994
Other overheads	234,433	181,034	157,919	200,518
	556,845	421,702	372,069	435,264
Operating profit before value added tax on financial services	301,910	217,299	228,194	339,471
Value added tax and NBT on financial services	37,456	41,309	25,231	45,755
Operating profit after value added tax on financial services	264,454	175,990	202,963	293,716
Share of associate company's profit before taxation				
Profit before taxation from operations				
Income tax expenses				
Profit for the year				
Other information				
As At 31st March				
Segment assets	11,093,954	9,925,519	6,184,745	6,825,676
Segment liabilities	8,766,056	7,686,927	4,886,971	5,286,219
Net assets	2,327,898	2,238,592	1,297,774	1,539,457

Operating Income



	2017	2016
A - Finance Lease	33	29
B - Hire Purchase	23	32
C - Loans & Advances	34	30
D - Investments	8	7
E - Others	2	2

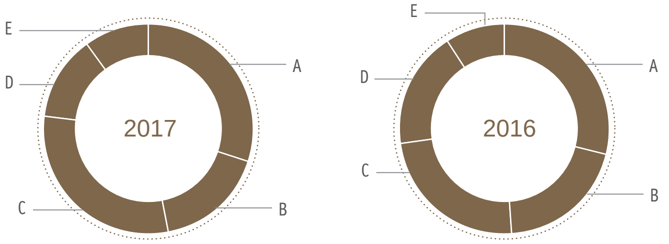
Operating Profit



	2017	2016
A - Finance Lease	32	25
B - Hire Purchase	25	41
C - Loans & Advances	4	12
D - Investments	(37)	19
E - Others	2	2

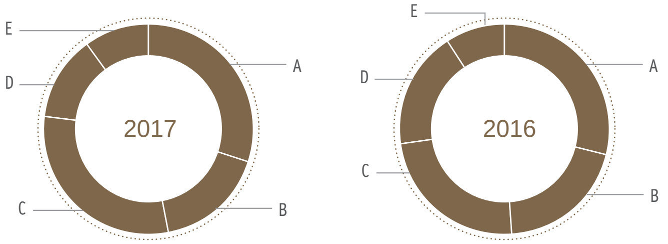
Loans & Advances		Investments		Others		Total	
2017	2016	2017	2016	2017	2016	2017	2016
Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000
1,919,319	1,395,042	230,389	129,749	-	-	5,286,060	4,301,828
1,066,224	666,504	259,391	61,990	68,291	43,110	(3,136,218)	2,098,378
853,095	728,538	(29,002)	67,759	(68,291)	(43,110)	2,149,842	2,203,450
-	-			83,622	58,927	83,622	58,927
-	-	59,542	5,143	-	-	59,542	5,143
-	-	177,001	103,072	-	-	177,001	103,072
-	-	-	-	39,308	31,305	39,308	31,305
853,095	728,538	207,541	175,974	54,639	47,122	2,509,315	2,401,897
246,308	198,289	443,736	-	-	-	625,066	234,816
606,787	530,249	(236,195)	175,974	54,639	47,122	1,884,249	2,167,081
240,663	168,988	28,888	15,717	15,415	10,929	678,232	532,029
23,021	17,727	-	-	-	-	110,120	117,536
24,550	15,879	2,947	1,477	1,572	1,028	69,186	49,994
9,840	3,817	1,181	355	630	247	27,731	12,019
240,103	191,672	28,821	17,827	15,381	12,392	676,657	603,443
538,177	398,083	61,837	35,376	32,998	24,596	1,561,926	1,315,021
68,610	132,166	(298,032)	140,598	21,641	22,526	322,323	852,060
38,362	43,736	9,333	7,460	2,456	2,830	112,838	141,090
30,248	88,430	(307,365)	133,138	19,185	19,696	209,485	710,970
						104,194	91,675
						313,679	802,645
						(111,665)	(297,626)
						202,014	505,019
11,366,577	8,302,333	4,943,028	6,033,417	3,904,360	2,877,762	37,492,664	33,964,707
8,981,474	6,429,833	3,905,809	4,672,645	3,085,089	2,234,852	29,625,399	26,310,476
2,385,103	1,872,500	1,037,219	1,360,772	819,271	642,910	7,867,265	7,654,231

Operating Assets



	2017	2016
A - Finance Lease	30	29
B - Hire Purchase	17	20
C - Loans & Advances	30	24
D - Investments	13	18
E - Others	10	9

Operating Liabilities



	2017	2016
A - Finance Lease	30	29
B - Hire Purchase	17	20
C - Loans & Advances	30	24
D - Investments	13	18
E - Others	10	9

Notes to the Financial Statements

52. Current and non-current analysis of assets and liabilities

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled.

As at 31st March	2017			2016		
	Within 12 months	After 12 months	Total	Within 12 months	After 12 months tax	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Assets						
Financial assets						
Cash and cash equivalents	1,244,554	-	1,244,554	344,062	-	344,062
Placement with banks	52,324	1,177	53,501	463,842	1,142	464,984
Financial investments-available for sale	3,080,212	813,340	3,893,552	3,852,148	788,967	4,641,115
Loans and receivables	5,931,338	5,435,239	11,366,577	4,355,208	3,947,125	8,302,333
Finance lease receivables	3,410,081	7,683,873	11,093,954	3,405,876	6,519,643	9,925,519
Hire purchase receivables	2,335,328	3,849,417	6,184,745	2,942,343	3,883,333	6,825,676
Other financial assets	169,608	276,178	445,786	110,440	-	110,440
Total financial assets	16,223,445	18,059,225	34,282,669	15,473,919	15,140,210	30,614,129
Non-financial assets						
Inventories	7,882	-	7,882	16,467	-	16,467
Current tax refunds	121,051	-	121,051	27,212	-	27,212
Investment in associates	-	995,977	995,977	-	927,318	927,318
Other assets	20,671	61,061	81,732	11,902	60,512	72,414
Property, plant and equipment	-	1,790,296	1,790,296	-	1,803,939	1,803,939
Leasehold property	-	42,140	42,140	-	42,608	42,608
Intangible assets	-	12,577	12,577	-	12,386	12,386
Investment property	-	158,340	158,340	-	448,234	448,234
Total non-financial assets	149,604	3,060,391	3,209,995	55,581	3,294,997	3,350,578
Total assets	16,373,049	21,119,616	37,492,664	15,529,500	18,435,207	33,964,707
Liabilities						
Financial liabilities						
Bank overdraft	1,092,434	-	1,092,434	412,472	-	412,472
Deposits due to customers	13,137,963	3,879,711	17,017,674	11,870,560	3,945,030	15,815,590
Debt instruments issued and other borrowings	7,286,980	2,878,857	10,165,837	4,943,846	3,583,323	8,527,169
Other financial liabilities	776,819	-	776,819	1,052,327	-	1,052,327
Total financial liabilities	22,294,196	6,758,568	29,052,764	18,279,205	7,528,353	25,807,558
Non-financial liabilities						
Deferred tax liability	-	361,223	361,223	-	343,259	343,259
Other liabilities	39,640	-	39,640	13,423	-	13,423
Retirement benefit obligation	-	171,772	171,772	-	146,235	146,235
Total non-financial liabilities	39,640	532,995	572,635	13,423	489,494	502,917
Total liabilities	22,333,836	7,291,563	29,625,399	18,292,628	8,017,847	26,310,475
Net assets/ liabilities	(5,960,787)	13,828,055	7,867,265	(2,763,128)	10,417,360	7,654,232

53. FINANCIAL RISK MANAGEMENT

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53.2 Introduction

Risk is inherent in MI's activities and, as a financial intermediary, the Company is exposed to various types of risks including credit, market, liquidity and operational risks which are inherent in the Company's activities. These risks are being managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. The Risk Management function strives to identify potential risks in advance, analysing them and it guides management to take precautionary steps to mitigate the impact of risk whilst optimising risk-adjusted returns within the Risk Appetite of the Company. This process of risk management is critical to the Company safeguarding its assets whilst continuing to generate profitability and each individual within the Company is accountable for the risk exposures relating to his or her responsibilities. MI's risk management process is streamlined in effect to ensure there is appropriate balance between risk and rewards. By instilling various controls and strategies, management continuously strives to mitigate risks in the attempt of generating higher profits. This note provides disclosure about MI's exposure to each identified key risks and outlines management process for the identification, measurement and monitoring of such risks and associated considerations.

53.3 Credit Risk

The financial loss resulting from a borrower or counterparty to a financial instrument failing or delaying to meet its contractual obligations is referred to as credit risk. Since MI possesses over Rs. 29 Billion loans and advances portfolio and other comparable financial instruments including investments in debt securities, MI is exposed to credit risk that need to be managed.

In managing credit risks which is deemed the main risk element for MI as a finance company, the Management takes into account all elements of credit risk exposures both at micro and macro levels to manage and control associated risks. MI considers and consolidates all elements of credit risk exposure (such as individual obliger default risk, province and sector concentration risks) to ensure stringent Credit Risk Management is in effect at all times eliminating or mitigating financial losses.

Notes to the Financial Statements

53.3.1 Key Definitions Related to Credit Risk Management

Impairment
This occurs when the recoverable amount of an asset is less than its carrying amount. Refer pages 305 to 306 in Notes to the financial statements for details on impairment methodology adopted and related policies.

Individual Impairment
Significant lendings are assessed individually for impairment. Assets are tested under individual impairment if the carrying value of the underlying asset is greater than a pre-determined threshold. The threshold specified at MI varies product category wise and this enables the Company to build defences against the risk of high exposure contracts defaulting on payments.

Past Due
MI considers that any amount uncollected one day or more beyond their contractual due date are ‘past due’.

Non-Performing Loans (NPL)
A loan placed on a cash basis (i.e. interest income is only recognised when cash is actually collected) after when six instalments or more are overdue, as there is reasonable doubt regarding the collectability of its instalments of capital and interest.

53.3.2 Credit Quality by Class of Financial Assets

A company specific credit quality categorisation method is adopted by MI based on available collateral buffer and loss rate indicators to ascertain the credit quality of financial assets. The table below sets out information about the maximum exposure to credit risk broken down according to financial assets by its class, based on the credit risk categorisation mechanism adopted by the Company as at the end of the financial year.

53.3.2.A. Credit quality by class of financial assets - as at 31st March 2017

As at 31st March	Neither past due nor impaired			Past due not impaired	Individually impaired	Total
	High Grade	Standard Grade	Low Grade			
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Financial Assets						
Cash & Short term Fund	1,244,554	-	-	-	-	1,244,554
Placements with the banks	53,501	-	-	-	-	53,501
Financial Investments - Available for sale	3,842,153	-	-	-	51,399	3,893,552
Other Financial assets	169,608	-	-	-	276,178	445,786
Hire Purchase receivable	3,910,677	240,004	448,885	1,393,081	443,723	6,436,370
Finance lease receivables	7,880,667	513,135	378,904	1,862,075	616,584	11,251,365
Loans & Advances	8,464,576	-	-	1,288,557	2,147,218	11,900,351
	25,565,736	753,139	827,789	4,543,713	3,535,102	35,225,480

Commentary
73% of MI's financial assets are of ‘high grade’ which are neither past due nor impaired mainly comprising of the lendings and financial investments – Available-for-sale. There is constant review of individual impaired past due not impaired and low grade accounts by MI's recovery division to sustain overall asset quality, taking appropriate recovery measures on a timely manner.

53.3.2.B. Past due (facilities in arrears of 1 day and above) but not impaired age analysis by class of financial assets - as at 31st March 2017

	Past due not impaired age analysis					Total
	< 30 days	31 to 60 days	61 to 90 days	91 to 120 days	120 & above	
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Hire purchase receivables	824,121	269,897	45,882	38,789	214,392	1,393,081
Finance leases receivables	1,167,996	414,126	71,228	43,075	165,650	1,862,075
Loans and advances	780,880	217,297	34,306	88,322	167,751	1,288,556
Total	2,772,997	901,320	151,416	170,186	547,793	4,543,712

53.3.2.C. Types of collateral taken to minimize credit risk exposure

Type of lending	Collateral generally obtained
Lease	Agricultural land and vehicles, Commercial property, Computer hardware and equipment, Dual purpose vehicles, Land vehicles, Motor bicycles, Motor cars, Motor coaches, Motor lorries, Motor Tricycles, Non- agricultural land vehicles, Other equipment, Other machinery, Prime movers, Tractor three wheels and tractor four wheels. From February 2017, the Loan to Value is kept at predetermined rates as directed by CBSL.
Hire Purchase	Same as above
Personal Loans/ Term Loans	Same as above except Residential property.
Micro Finance	Promissory notes

Type of Collateral	Value of Collateral - as at 31st March 2017			
	Hire Purchase	Lease	Personal Loans/ Term Loans	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Dual Purpose Vehicles	1,721,563	2,434,663	1,425,464	5,581,690
Motor Cars	2,374,147	5,648,007	5,640,875	13,663,029
Motor Coaches	352,598	733,450	219,111	1,305,159
Motor Lorries	1,152,586	766,627	276,223	2,195,436
Others	836,779	1,667,319	2,484,199	4,988,297
Properties	-	-	1,854,476	1,854,476
	6,437,673	11,250,066	11,900,348	29,588,087

As an additional safeguard, guarantors are requested particularly for lease and hire purchase business. The Company resorts to repossession of assets kept as security when the borrowers default goes beyond the specified credit period. The sales proceeds resulting from the subsequent sale of such assets are then used to minimise credit risk exposure.

53.3.3 Analysis of Risk Concentration

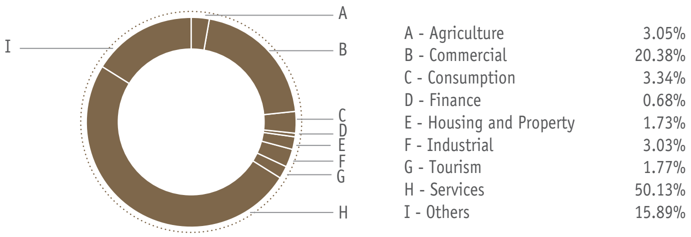
The Company monitors its credit concentration risk by referring to the degree of credit exposure by MI to various sectors and by geographic locations.

53.3.3.A. Sector Wise Analysis

Outlined below are the maximum credit exposures of MI's loans and advances to various sectors, as at the end of the financial year:

Concentration by Sector	As at					
	31.03.2017	%	31.03.2016	%	31.03.2015	%
	(Rs. 000)		(Rs. 000)		(Rs. 000)	
Agriculture	901,570	3.05	854,582	3.31	689,826	3.43
Commercial	6,031,322	20.38	5,431,608	21.03	3,950,030	19.62
Consumption	987,308	3.34	813,470	3.15	534,806	2.66
Finance	202,054	0.68	171,595	0.66	99,679	0.49
Housing and Property	512,207	1.73	695,059	2.69	314,565	1.56
Industrial	896,456	3.03	852,889	3.3	706,636	3.51
Tourism	525,114	1.77	3,851,287	14.91	3,099,147	15.4
Services	14,832,278	50.13	12,805,217	49.57	10,441,629	51.85
Others	4,699,778	15.89	354,366	1.4	300,951	1.5
Total	29,588,087	100	25,830,073	100	20,137,269	100

Notes to the Financial Statements


Sector Wise Credit Concentration 2016/17

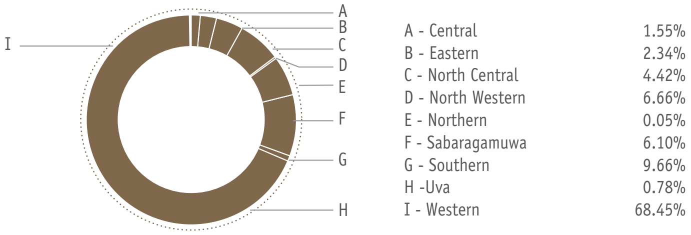
Commentary

There is a high percentage lending to Services sector reaching 50% of total lending mainly attributed to lendings carried out for transportation services. Management would monitor risk levels attached to these sectors on an ongoing basis. Currently, these sectors do not pose any significant risk. LTV limitations for vehicle backed lending increases collateral cover, minimising credit exposure to such sectors.

53.3.3.B. Province Wise Analysis

This table below discloses MI's credit exposure to various provinces based on the lending carried out by MI's branch network that is geographically scattered across the country:

Concentration by Province			**As at**			
	31.03.2017	**%**	**31.03.2016**	**%**	**31.03.2015**	**%**
	(Rs. 000)		**(Rs. 000)**		**(Rs. 000)**	
Western	20,251,692	68.45	18,487,624	71.57	14,718,811	73.09
Central	459,415	1.55	312,311	1.21	225,143	1.12
Eastern	691,269	2.34	651,661	2.52	548,360	2.72
North Central	1,307,575	4.42	1,035,443	4.01	710,440	3.53
North Western	1,971,525	6.66	1,571,683	6.08	1,066,584	5.3
Northern	13,994	0.05	5,838	0.02	9,567	0.05
Sabaragamuwa	1,803,641	6.10	1,418,995	5.49	932,299	4.63
Southern	2,857,324	9.66	2,105,357	8.15	1,705,543	8.47
Uva	231,652	0.78	241,160	0.93	220,522	1.1
Total	**29,588,087**	**100%**	**25,830,072**	**100%**	**20,137,269**	**100%**


Province Wise Credit Concentration 2016/17

Commentary

MI's lending is mainly concentrated around the Western Province with a 68% contribution towards total lending, with a slight decrease compared to last year's 72%. In keeping to MI's expansion strategy and volume growth expectation outside the Western Province, there is already a clear indication of diversification to other regions, in particular the Southern, Central, North Western and Sabaragamuwa Provinces.

53.3.4 LOAN TO VALUE RATIO (LTV)

LTV ratio is a computation that expresses the amount of a first disbursement as a percentage of the total appraised value of assets kept as security usually being its market value. The two tables below states the average LTV ratio's asset category wise based on regulations issued by CBSL.

Based on CBSL Directions No. 01 of 2017 and No. 02 of 2017 on Loan to Value Ratio for Credit facilities in respect of Motor Vehicles;

From 1st April 2016 to 31st January 2017

Contract Type	Motor Vehicles average LTV Ratio %
Hire Purchase	58.71
Lease	58.93
Vehicle Loans	54.63
Other Loans	58.67

From 1st February 2017 to 31st March 2017

LTV Category	CBSL requirement %	Total %
Vehicles For Tourism / Transportation	100	72.96
Three Wheelers/ Un-Registered Or Registered in Sri Lanka less than 12 Months	25	23
For Motor Cars / SUV's /Vans / Un-Registered Or Registered in Sri Lanka less than 12 months	50	44.84
Other Vehicles / Un-Registered Or Registered in Sri Lanka less than 12 months	70	60.6
For Commercial Vehicles / Un Registered Or Registered in Sri Lanka less than 12 months	90	70.05
Any Vehicle registered in Sri Lanka more than 12 months	70	58.58

53.4 Liquidity Risk

Liquidity risk is defined as the risk that the Company may encounter difficulties in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises because of the possibility that the Company might be unable to meet its payment obligations when they fall due under both normal and stress circumstances. MI has implemented strict policies on managing of its assets, keeping liquidity as a vital focus, monitoring the liquidity position on a daily basis through the Finance division under the leadership of the Finance Director. To limit this risk, management has arranged diversified funding sources in addition to its deposit base, and adopted a policy of managing liquidity by monitoring future cash flows and assets and liabilities positions on an on-going basis.

To strengthen liquidity management, MI Board has established the Assets and Liability Management Committee (ALCO) to oversee liquidity risk aspects associated with MI's businesses from a macro perspective, while treasury department is responsible for the day to day management of liquidity. The IRMC was formed soon after CBSL issued the Corporate Governance Direction in 2013. The committee's duties include an independent review of the effectiveness of the liquidity risk management process and recommending suitable actions when necessary to the Board and the management.

The three year strategic plan devised projects the medium term cash flow position so that appropriate strategic measures could be devised to manage future liquidity requirements. During the year, in managing short and medium term funding needs, the Treasury Division resorted to borrowing to mobilise funds in addition to encouraging deposits mobilisation as its primary source of funding. (Refer Financial Capital Treasury Section on page 76)

53.4.1. Exposure to Liquidity Risk

Ratio	2017	2016	2015
Net Loans/ Customer Deposits	168%	158%	142%
Net Loans/ Total Assets	76%	74%	69%

Commentary

MI's net loans to deposits ratio has increased and is at 168% and Management plans to bring this ratio below 140% as per forecast within the next financial year with the planned growth in deposits.

Notes to the Financial Statements

53.4.2 Financial Assets and Liabilities by Remaining Contractual Maturities

The following tables show the maturity gap analysis of MI’s financial assets and financial liabilities based on their remaining period to maturity undiscounted as at 31st March 2017.

For the year ended 31st March	On demand	Up to 3 Months	4-12months	1 to 3 Years	3 to 5 Years	More than 5 Years	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Assets							
Financial Assets							
Cash and cash equivalents	1,244,554	-	-	-	-	-	1,244,554
Placement with banks	-	15,427	36,896	-	-	1,178	53,501
Financial investments available for sale		2,555,453	524,758		83,181	730,160	3,893,552
Loans and receivables	-	1,140,682	4,790,656	4,061,307	1,367,218	6,714	11,366,577
Finance lease receivables	-	1,078,480	2,331,601	5,992,014	1,691,707	152	11,093,954
Hire purchase receivables	-	779,795	1,555,533	2,915,042	934,375		6,184,745
Other financial assets	-		169,607		-	276,179	445,786
Inventories	-	7,460	422	-	-	-	7,882
Current tax refunds	-	-	81,732	-	-	-	81,732
Investment in associates	-	-	-	-	-	995,977	995,977
Total Financial Assets	1,244,554	5,577,297	9,491,205	12,968,363	4,076,481	2,010,360	35,368,260
Liabilities							
Financial Liabilities							
Bank Overdraft	-	873,947	218,487	-	-	-	1,092,434
Deposits Due to Customers	-	5,574,360	7,563,604	2,857,345	1,022,365	-	17,017,674
Debt Instruments Issued and Other Borrowings	-	3,435,158	3,851,822	2,335,535	543,322	-	10,165,837
Other Financial Liabilities	-	425,890	350,929	-	-	-	776,819
Deferred Tax Liability	-	-	-	-	-	361,223	361,223
Total Financial Liabilities	-	10,309,355	11,984,842	5,192,880	1,565,687	361,223	29,413,987
Net Financial Assets/Liabilities	1,244,554	(4,732,058)	(2,493,637)	7,775,483	2,510,794	1,649,137	5,954,273

Commentary

In a rising interest rate scenario deposit placed tended to be of a short term nature, while majority of lending continued to be of a longer tenor(4 to 5 years). This has resulted in the less than 1 year maturity gap widening to Rs. 5.9 Bn.

Based on the ALCO recommendations treasury and deposit divisions in tandem is pursing longer term funding at optimal pricing.

53.4.3 Performance in Statutory Liquidity Position

Liquidity position is monitored on a daily basis and this includes meeting daily cash requirements and the maintaining of the minimum statutory liquidity position. The Board is appraised of MI’s liquidity position on a monthly basis and periodic statutory liquid assets reports are also submitted to the regulator on due dates. MI has maintained its statutory liquid assets ratio above the minimum requirements specified by the regulator.

To comply with the Liquid Assets Direction No. 4 of 2013, MI’s liquidity shall not be less than the total of;

(a) 10% of the outstanding value of the time deposits and accrued interest payable at the close of the business on such day and

(b) 15% of outstanding value of the saving deposit and accrued interest payable at the close of the business on such day and

(c) 10% of the total outstanding borrowing and any payable.

A shortfall arose in minimum approved securities in the form of Sri Lankan Government securities equivalent to 7.5% of the average of its month end total deposit liabilities and borrowings of the 12 months preceding financial year due to the impairment of investment in repurchase agreement with a primary dealer appointed by the Central Bank of Sri Lanka. However, subsequent to the reporting date, the company has invested in government securities to meet the requirement as per the Liquid Assets Direction No.04 of 2013.

53.4.4 Key Definitions Related to Liquidity Risk Management

Liquid Assets
Assets that are held in cash or in a form that can be converted to cash readily, such as deposits with banks free from any charge or lien and treasury bills and bonds.

Liquid Asset Ratio
Assets that are held in cash or in a form that can be converted to cash readily (as prescribed by the Central Bank of Sri Lanka) divided by the total deposits and outstanding borrowings excluding secured borrowings and borrowings considered as capital funds.

	CBSL minimum requirement as at 31st March 2017	Actual 31st March 2017	CBSL minimum requirement as at 31st March 2016	Actual 31st March 2016
Total liquid assets (Rs.000)	1,724,423	1,861,433	1,605,562	1,881,722
Statutory liquid assets ratio (%)	10%	10.81%	10%	11.73%
Minimum approved securities (Rs.000)	1,147,357	563,377	1,024,132	1,070,924

*Note: The shortfall in investments in minimum approved securities arising from the matter given in note no 26.1 to the financial statements was bridged in the next Financial Year.

53.4.5 Daily Liquidity Management

Based on funding requirements, to meet daily lending and expenditure, treasury manages cash flows by obtaining funding lines and temporary facilities from banks and other financial intermediaries. To avail as funds, the total unutilised credit lines stood at Rs. 1.63 Billion as at 31st March 2017. To boost funding deposit mobilisation was the primary funding option. The Company stresses the importance of savings accounts as sources of funds to finance lending to customers. MI monitors the advances to deposit ratio, which compares loans and receivables to customers as a percentage of customer savings accounts and fixed deposits to ensure an optimal blend is maintained.

53.5 Market Risk

Market risk is the risk of losses resulting from On or Off-Balance Sheet positions arising out of movements in prices affecting interest rate, foreign exchange exposures and equity prices. MI's market risk exposure primarily revolves around interest rate risk and equity price risk. MI is not exposed to exchange rate risk presently, due to no marketed negligible transactions being recorded.

53.5.1 Interest Rate Risk

The possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments gives rise to interest rate risk. MI's policy is to continuously monitor portfolios, evaluate interest rate shocks to profitability and adopt hedging strategies to ensure that interest rate risk is maintained within prudent levels. To keep interest rate risk moderate, MI's risk management function assists in analysing interest rate trends and predicting cycles so that we enter into transactions without unnecessarily exposing MI to such risks. In analysing impacts of interest rate on profitability, we analyse MI's interest rate sensitivity level based on the Company's exposure to various financial assets and liabilities in terms of interest payments. MI manages its interest rate risk by having a balanced portfolio of fixed and variable rate financial assets and financial liabilities. Managing the assets and liability mismatch is also looked at from a macro perspective to manage the risk.

53.5.1.A. Interest Rate Sensitivity Analysis

Given below is a sensitivity analysis carried out as at 31st March 2017 that demonstrates possible impact to MI's Income Statement due to a given change in interest rates, keeping all other variables constant.

	Market Rates up by 0.5% effect to the Interest Income / (Expenses)	Market Rates drop by 0.5% effect to the Interest Income/ (Expenses)	Market Rates up by 1% effect to the Interest Income / (Expenses)	Market Rates drop by 1% effect to the Interest Income/ (Expenses)
	(Rs. 000)	**(Rs. 000)**	**(Rs. 000)**	**(Rs. 000)**
Effect on Rate sensitive Assets	177,382	(177,382)	354,764	(354,764)
Effect on Rate sensitive Liabilities	(147,414)	147,414	(294,828)	294,828
Sensitivity/ effect to Income statement	29,968	(29,968)	59,936	(59,936)

Commentary

MI possesses interest rate sensitive assets of Rs. 35.5 billion and interest rate sensitive liabilities of Rs. 29.6 billion. Currently the impact from an interest rate fluctuation of 1%+ or (1%) is moderate.

Notes to the Financial Statements

Assumptions and Limitations

- The interest rates movements have been applied on the basis that both assets and liabilities pricing rates are on a fixed basis. i.e. Assumed no floating rates applicable.
- The market rates are predicted not to change materially in the foreseeable future.
- The lending and deposit volumes are assumed to remain unchanged.

53.5.1.B. Financial Assets and Financial Liabilities Exposed to Interest Rate Risk

Disclosed below are the Company's financial assets and financial liabilities exposed to interest rate risk as at 31st March 2017. The financial assets and financial liabilities so disclosed are at their carrying amounts and categorised by the earlier of contractual re-pricing or maturity dates.

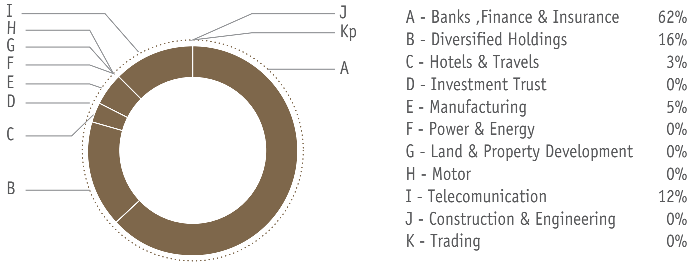
For the year ended 31st March	Up to 3 months	3 to 12 months	1 to 3 Years	3 to 4 Years	4 to 5 Years	More than 5 Years	Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Financial Assets							
Placement with Banks	15,427	36,896	-	-	-	-	52,323
Financial Investments Available for Sale	48,820	514,558	-	17,142	66,039	112,146	758,705
Loans and Receivables	393,781	3,855,971	2,457,102	1,684,846	1,568,568	58,727	10,018,995
Finance Lease Receivables	18,495	250,170	4,490,763	3,986,644	2,252,587	886	10,999,545
Hire Purchase Receivables	24,978	359,990	2,861,358	1,712,154	1,058,923	-	6,017,403
Total Financial Assets	501,501	5,017,585	9,809,223	7,400,786	4,946,117	171,759	27,846,971
Liabilities							
Financial Liabilities							
Bank Overdraft	1,092,434	-	-	-	-	-	1,092,434
Deposits Due to Customers	5,574,360	7,563,604	2,857,345	1,022,365	-	-	17,017,674
Debt Instruments Issued and Other Borrowings	2,600,109	1,523,985	3,984,234	2,057,509	-	-	10,165,837
Total Financial Liabilities	9,266,903	9,087,589	6,841,579	3,079,874	-	-	28,275,945
Interest Sensitivity Gap	(8,765,402)	(4,070,004)	2,967,644	4,320,912	4,946,117	171,759	(428,974)

53.5.2 Equity Risk

Equity price risk arises as a result of any change in prices and volatilities of individual equities held by MI. Having an equity investment base of Rs. 3 Billion, the Company could be exposed to equity risk. Equity investment value could decline because of the share prices declining due to adverse events impacting the stock market. MI keeps close watch on movements in share prices to ascertain equity risk and to manage the portfolio to derive maximum returns while minimising losses. MI possesses a well-diversified share portfolio that has been primarily invested in large blue chip institutions mostly in the hotel and banking sector. MI conducts mark-to-market calculations on a weekly, monthly and quarterly basis to identify fair value impacts due to changes in equity prices.

To minimise equity risk, MI monitors the performance of the stock market and identifies existing conditions, identified trends and makes predictions and then base investments and disposal decisions on an on-going basis. The Risk Manager, Management and the IRMC ascertain potential equity risk and propose remedial action as deemed necessary and reports findings to the Board.

Effect to the Comprehensive Statement of Income
If Market Drops to the Recorded Lowest Market Price



53.5.2.A. Analysis on Exposure to Equity Price Risk

Impact on Other Comprehensive Income due to change in market price by 10% on equity shares held by the Company.

The sensitivity analysis for equity risk reflects how changes in the fair value of equity securities at the reporting date will fluctuate in response to assumed changes in equity market prices. The movements in the fair value of equity securities are monitored by assessing the projected changes in the fair value of equity securities held by the portfolios in response to assumed equity price movements of 10% on equity price upward or downward.

The table below summarises the impact (both to the Income Statement and to the equity) due to a shock of 10% on equity price.

	2016/17	2015/16
	Available-for-Sale	Available-for-Sale
	Rs. '000	Rs. '000
Market value of equity securities as at 31st March 2017		
Stress Level	Impact on OCI	Impact on OCI
Shock of 10% on equity price (upward)	305,402	329,252
Shock of 10% on equity price (downward)	(305,402)	(329,252)

Commentary

The Company carried out a risk analysis on its share portfolio based on possible downward market changes, considering the last five years lowest market prices recorded in the Colombo Stock Market for this financial year. Based on this analysis, the maximum amount of equity risk effect to the other comprehensive statement of income is Rs. 555 Million as at the end of 31st March 2017. Company disposed a part of it's investment subsequent to the balance sheet date to manage the risk.

Notes to the Financial Statements

53.6 Operational Risk

Operational risk arises due to inadequate or failed internal processes, people and systems or from external events. Operational risk events which include legal and regulatory implications could lead to financial and reputational losses to MI. When managing operational risk, the Company strives to maintain an appropriate operational balance by avoiding financial losses and damage to MI's reputation because of poor operational procedures and practices, whilst ensuring overall cost effectiveness of selecting right policies and procedures, avoiding control procedures which restrict initiative and creativity.

A clear Operational Risk Management Framework of MI has been defined by the Board (Refer page 259 on Risk Report). Operational risk is managed by establishing an appropriate internal control system that requires a mechanism for segregation of related responsibilities within the organisation, and a detailed testing and verification of the organisation's overall operational systems, and achieving a full harmony between internal and external systems and establishing a back-up facility for Business Continuity Planning. Independent higher level oversight and audit monitoring ensures compliance to operational policies, procedures and control.

Refer Risk Report on pages 258 to 260 Operational Risk for further disclosure.

53.6.1. Nature of Relationship Between The Associate and The Company

MI has a stake of 26.12% of Nuwara-Eliya Hotels, and the hotel is an associate of the Company. Currently, Nuwara-Eliya being in the tourism sector is enjoying steady profitability growth considering the positive economic environment towards tourism and the increasing influx of tourist arrivals to the country. MI expects this positive scenario to prevail in the foreseeable future, minimising associated risk to a significant degree.

53.6.2. Defined Benefit Plans Associated Risk

For purpose of assessing risk associated with employee benefit plans annually, the Company obtains support of an Independent expert to identify specific risk and make actuarial valuations and then to incorporate same in the Financial Statements.

Financial Statements Note 2.11.7, provides detailed breakdowns of estimates including assumptions made.

53.7 Capital Management

53.7.1 Objective

The Company manages its capital requirement taking into account the need to meet minimum regulatory capital needs and to maintain a capital buffer against unexpected losses as well as to cater to the current and future business needs, stakeholder expectations and to seek available options for raising and generating capital.

For MI, Capital Management is deemed a pivotal assessment exercise in sustaining an adequate buffer against losses arising from any unforeseen risks. Hence, management monitors MI's capital adequacy position closely through the Finance Division and reports to the Board monthly. Capital adequacy is a measure of the Company's ability to tolerate associated risks in doing its finance business. The main objective of maintaining adequate capital in terms of regulatory capital adequacy ratios is to safeguard the depositors, while sustaining customer confidence. The capital adequacy measurement being a widely accepted concept specifies the limit up to which MI can expand in terms of its risk weighted assets. In pursuit of business expansion and diversification, MI engages itself in activities dealing in financial instruments that regularly change the risk and capital profile of the Company. Thus regulatory capital requirements ensure company does not move into undue expansion beyond specified limits and signals the Company to be cautious and not to take undue risk through growth of its assets especially in areas risky than others.

The Company over its fifty year history has managed to accumulate a sound capital position, which stands at Rs. 8 Billion. In this context, MI's capital strength serves as a cushion in absorbing any unexpected losses that may arise and is a good indicator of MI's levels of safety towards stakeholders more importantly its depositors. MI's policy on capital is to retain a strong capital base at all times so as to ensure investor, creditor and market confidence and to back the sustainable growth of the Company.

MI reviews its Capital Adequacy Ratios (CAR) on a monthly basis to ensure compliance to prudential requirements on capital. The Company's Core Capital Ratio and Total Risk Weighted Capital Ratio (TRWCR) were maintained well above the minimum regulatory requirements of 5% and 10% respectively throughout 2016/17 financial period.

The computation of the CAR ratios is in two parts and involves firstly a working to arrive at the Tier 1 capital and the capital base for the two ratios CCR and TRWCR respectively. A separate computation is carried out to derive at the total Risk Weighted Assets as at a given date.

The capital base comprises of two elements, namely Tier 1 and Tier 2 capital.

Tier 1 capital comprises the stated capital, statutory reserve fund, retained profits, general and other reserves excluding the revaluation reserve.

Tier 2 capital consists of the revaluation reserve of which only 50% could be taken for the computation. Other Tier 2 components include the general provision, approved subordinated term debts and other hybrid capital instruments. The Tier 2 capital is not allowed to exceed 100% of the Tier 1 capital for the Total Risk Weighed Capital Ratio. In deriving at the Total Risk Weighted Assets, each asset category in the balance sheet is arranged in the order of their risk and available security and thereafter pre-defined risk weights are assigned to each such category to compute the total risk weighted value.

53.7.2.A. Total Risk Weighted Asset Computation

	Principal amount of On-Balance Sheet Items	**Credit Equivalent of Off-Balance Sheet Items**	**Total**	**Principal amount of On-Balance Sheet Items**	**Credit Equivalent of Off-Balance Sheet Items**	**Total**	**Risk Weight Factor %**	**Risk Weighted Balance**	
Assets as at 31st March	**2017**			**2016**				**2017**	**2016**
	Rs. '000	**Rs. '000**	**Rs. '000**	**Rs. '000**	**Rs. '000**	**Rs. '000**		**Rs. '000**	**Rs. '000**
Cash and Cash Equivalents	1,244,554	-	1,244,554	344,062	-	344,062	0	-	-
Government debt securities	758,705	-	758,705	1,267,768	-	1,267,768	0	-	-
Financial Investments - Available for Sale	2,727,397	-	2,727,397	2,781,245	-	2,781,245	100	2,727,397	2,781,245
Placements with Bank	53,501	-	53,501	464,984	-	464,984	20	10,700	92,997
Loans against fixed deposits	203,473	183,842	387,315	169,408	182,635	352,043	0	-	-
Loans and Advances	28,120,073	-	28,120,073	24,864,924	-	24,864,924	100	28,120,073	24,864,924
Inventories	7,882	-	7,882	16,467	-	16,467	100	7,882	16,467
Other Assets	648,570	-	648,570	210,066	-	210,066	100	648,570	210,066
Investments Properties	158,340	-	158,340	448,235	-	448,235	100	158,340	448,235
Property, Plant and Equipment	1,845,014	-	1,845,014	1,858,934	-	1,858,934	100	1,845,014	1,858,934
Total Risk Weighted Assets	35,767,509	183,842	35,951,351	32,426,093	182,635	32,608,728		33,517,976	30,272,868

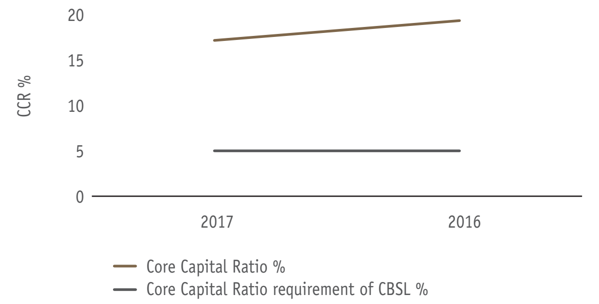
53.7.2.B. Total Capital Base Computation

As at 31st March	**2017**	**2016**
	Rs.'000	**Rs.'000**
Tier 1: Core Capital		
Stated capital	36,000	36,000
Statutory Reserve fund	661,400	631,400
General reserve	4,067,234	3,980,846
Retained earnings	989,196	1,210,116
Total Tier 1 Capital	5,753,830	5,858,362
Tier 2: Supplementary Capital		
Revaluation Reserves(as approved by CBSL)	428,012	428,012
Total Tier 2 Capital	6,181,842	6,286,374
Less		
Investments in capital of other banks/financial associates	(1,403,427)	(1,519,420)
Capital Base	4,778,415	4,766,954

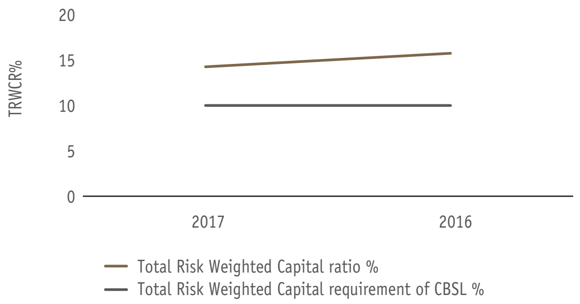
Notes to the Financial Statements

53.7.2.C. Capital Adequacy Ratios

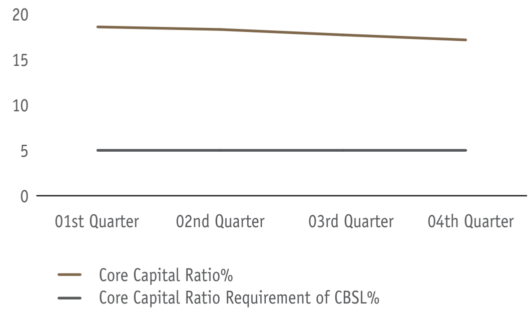
As at 31st March		**2017**	**2016**
		%	**%**
Core Capital Ratio	= $\frac{\text{Tier 1 Capital}}{\text{Risk Weighted Assets}}$	17.17	19.35
Total Risk Weighted Capital Ratio	= $\frac{\text{Capital Base}}{\text{Risk Weighted Assets}}$	14.26	15.75



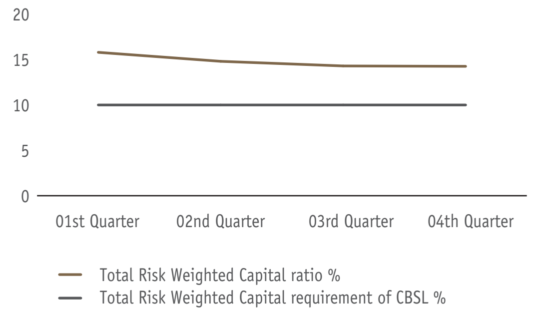
Core Capital Ratio - Annual



Total Risk Weighted Capital Ratio - Annual



Core Capital Ratio - Quarterly (%)



Total Risk Weighted Capital Ratio -Quarterly (%)

53.7.3 Performance in Capital Adequacy Position

MI's capital adequacy ratios are well above the statutory limits at least by a 4% margin. The Company's capital adequacy ratios have remained intact from last year due to the generation of sound internally generated profits. MI is fortunate to possess this strong capital position on account of continued growth in accumulated retained earnings achieved by posting consistent annual profits for the last number of years.

	CBSL minimum requirement as at 31st March 2017	**Actual 31st March 2017**	**CBSL minimum requirement as at 31st March 2016**	**Actual 31st March 2016**
Total Tier I capital (Rs. 000)	1,676,116	5,753,830	1,512,287	5,858,362
Total Capital Base (Rs. 000)	3,352,232	4,778,415	3,024,574	4,766,954
Core Capital Ratio (%)	5	17.17	5	19.35
Total risk Weighted Capital Ratio (%)	10	14.26	10	15.75

*Based on statutory basis reporting balances

Additional Information

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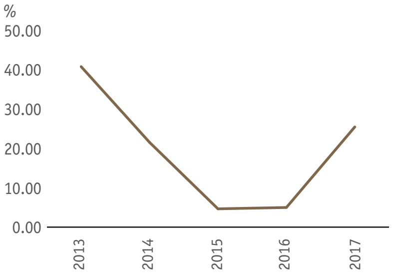
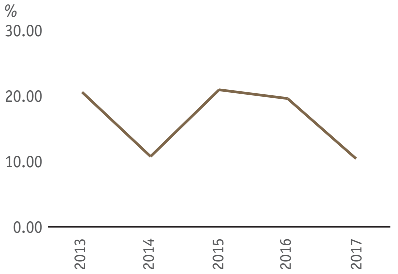
Decade at A Glance

	Based on SLFRS/LKAS							Based On SLAS		
For the year ended 31st March	**2017**	**2016**	**2015**	**2014**	**2013**	**2012**	**2011**	**2010**	**2009**	**2008**
	Rs.000	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**
Operating Results										
Income	5,645,532	4,500,275	4,286,288	4,095,811	3,370,086	2,394,235	2,214,120	1,806,966	1,708,609	1,372,133
Interest expense	3,136,218	2,098,378	1,947,783	2,215,483	1,867,700	1,009,874	679,728	791,308	989,662	720,125
Non Interest expenses	2,299,829	1,690,927	1,540,416	1,055,997	770,317	726,397	485,795	574,623	464,225	420,723
Profit before tax	313,679	802,645	911,884	824,331	732,069	625,755	1,048,597	441,035	254,409	231,285
Provision for taxation	111,664	297,626	280,612	148,969	101,278	15,667	142,699	112,436	21,034	82,716
Net profit for the year	202,014	505,019	631,272	675,362	630,791	610,088	905,898	328,600	233,375	148,569
Dividends	-	21,042	88,677	30,060	82,665	66,132	30,000	13,800	9,750	14,049
As at 31st March										
Assets										
Liquid assets	1,861,433	1,879,970	1,773,833	1,455,405	1,389,107	787,268	522,280	483,483	462,636	416,332
Investments	3,319,973	3,559,791	4,202,760	2,892,173	2,980,019	3,390,331	4,779,213	1,761,332	930,836	1,196,974
Debentures	10,200	10,400	10,700	10,700	10,773	-	-	-	-	2,232
Advances	28,645,275	25,053,528	19,468,293	16,187,399	13,844,647	10,446,514	6,416,176	4,430,395	5,205,265	5,377,167
Other assets	656,452	226,532	157,544	419,479	718,304	741,769	271,242	309,509	217,281	268,717
Property, plant & equipment	1,790,296	1,803,939	1,756,125	1,709,676	1,535,732	1,565,620	1,214,750	1,037,007	1,015,271	888,378
Leasehold Property	42,140	42,609	43,076	43,545	44,013	44,481	44,950	45,418	45,886	-
Intangible Assets	12,578	12,386	3,344	3,714	4,681	2,855	6,521	-	-	-
Investment Property	158,340	448,234	198,769							
Investment in Associates	995,977	927,318	794,381	777,127	695,670	628,397	493,555	456,363	-	-
Total Assets	37,492,664	33,964,707	28,408,825	23,499,218	21,222,946	17,607,235	13,748,687	8,523,507	7,877,174	8,149,800
Liabilities										
Bank overdraft	1,092,434	412,472	272,634	279,269	999,036	505,815	397,246	213,395	625,709	765,175
Borrowings	10,165,837	8,527,169	5,682,640	4,917,129	5,232,331	4,638,644	2,318,481	403,599	1,236,670	1,679,362
Deposits from customers	17,017,674	15,815,590	13,720,729	11,417,741	8,424,720	6,137,896	4,297,801	3,479,291	2,774,974	2,409,257
Other liabilities	1,349,453	1,555,245	953,057	618,694	860,501	850,274	442,081	651,206	545,411	583,950
	29,625,399	26,310,476	20,629,060	17,232,833	15,516,588	12,132,629	7,455,609	4,747,491	5,182,764	5,437,744
Share Holder's Fund										
Share Capital	36,000	36,000	36,000	36,000	36,000	36,000	36,000	30,000	30,000	30,000
Reserves	7,831,265	7,618,231	7,743,765	6,230,385	5,670,358	5,438,606	6,257,078	3,746,016	2,664,410	2,682,056
	7,867,265	7,654,231	7,779,765	6,266,385	5,706,358	5,474,606	6,293,078	3,776,016	2,694,410	2,712,056
Total Share Holder's Funds & total liabilities	37,492,664	33,964,707	28,408,825	23,499,218	21,222,946	17,607,235	13,748,687	8,523,507	7,877,174	8,149,800

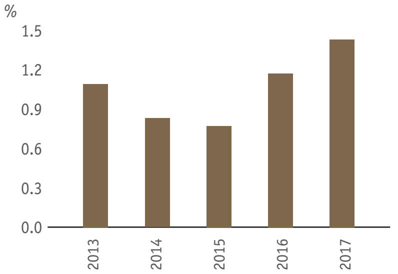
Growth in Income



Growth in Total Assets

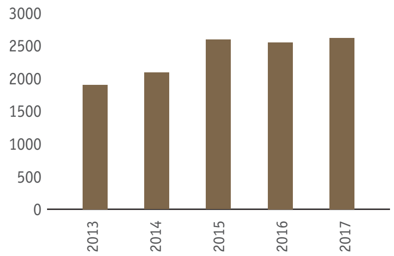


Debt to Equity

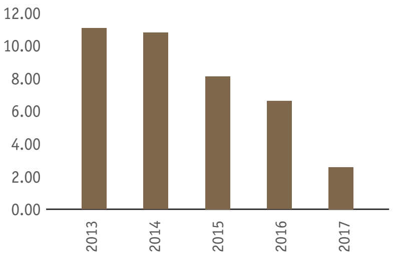


For the year ended 31st March	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
Financial Position										
Total Assests to Shareholders funds - (Times)	4.77	4.44	3.65	3.75	3.72	3.22	2.18	2.26	2.92	3.01
Debt to Equity - (Times)	1.43	1.17	0.77	0.83	1.09	0.94	0.43	0.16	0.69	0.90
Liquid assets as a % of deposits	10.94	11.89	12.93	12.75	17.00	13.00	12.00	14.00	17.00	17.00
Investor										
Return on shareholders' funds - (%)	2.57	6.60	8.11	10.78	11.05	11.14	14.40	8.70	8.66	5.48
Return on Average Assets - (%)	0.57	1.62	2.43	3.02	3.25	3.89	8.13	4.01	2.91	1.90
Net Assets per share - (Rs.)	2,616.87	2,546.32	2,588.08	2,084.63	1,898.32	1,821.23	2,093.51	1,258.67	898.14	904.02
Earnings per Share - (Rs.)	67.20	168.00	210.00	224.67	209.84	202.96	301.36	109.53	77.79	49.52
Dividend per Share - (Rs.)	-	7.00	29.50	20.00	27.50	22.00	9.98	4.60	3.25	4.68
Dividend Cover - (Times)	-	24.00	7.12	11.23	7.63	9.23	30.20	23.81	23.94	10.58
Dividend Payout - (%)	-	4.17	14.05	8.90	13.10	10.84	3.31	4.20	4.18	9.46
Interest Cover - (Times)	1.10	1.38	1.47	1.37	1.39	1.62	2.54	1.56	1.26	1.32
Growth										
Growth in income - (%)	25.45	4.99	4.65	21.53	40.76	8.13	22.53	5.76	24.52	25.61
Growth in Interest Expenses - (%)	49.46	7.73	-12.08	18.62	84.99	48.57	-14.10	-20.04	37.43	61.08
Growth in Other Expenses - (%)	36.01	9.77	45.87	37.09	6.05	49.53	-15.46	-23.78	10.34	36.62
Growth In Profit before Tax - (%)	-60.92	-11.98	10.62	12.60	16.99	-40.32	137.76	73.36	10.00	-31.43
Growth in Profit after Tax - (%)	-60.00	-20.00	-6.53	7.07	3.39	-32.65	175.68	40.80	57.08	-37.31
Growth In Total Assets - (%)	10.39	19.56	20.89	10.73	20.54	28.06	61.30	8.21	-3.35	8.54
Growth in advances - (%)	14.34	28.69	20.27	16.92	32.53	62.82	44.82	-14.89	-3.20	11.02
Growth in Deposit Base - (%)	7.60	15.27	20.17	35.53	37.26	42.81	23.53	25.38	15.18	16.63
Growth in Shareholders Funds - (%)	2.78	-1.61	24.15	9.81	4.23	13.01	66.66	40.14	-0.65	4.99
Statutory Ratios										
Core Capital Ratio - (Minimum 5%)	17.17	19.35	21.70	22.52	20.83	22.4	28.5	30.52	24.02	20.5
Risk Weighted Capital Ratio - (Minimum 10%)	14.26	15.75	15.27	17.32	22.4	27.17	34.69	38.82	30.26	35.12
Liquid assets %	10.81	11.73	12.45	12.78	17.11	12.86	12.78	13.85	16.89	17.28

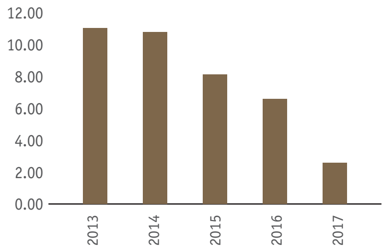
Net Assets Per Share



Return on Shareholders' Funds



Total Assets to Shaeholders' Funds



Quarterly Analysis

Statement of Profit or Loss

	1st Quarter		2nd Quarter	
	Apr-Jun 16	Apr-Jun 15	July-Sep 16	July-Sep 15
	Rs. 000	Rs. 000	Rs. 000	Rs. 000
Interest Income	1,185,169	979,968	1,315,226	1,044,768
Interest Expense	(635,474)	(476,579)	(775,910)	(498,291)
Net Interest Income	549,695	503,389	539,316	546,477
Fee and Commission Income	17,924	13,482	17,823	14,701
Net Fee and Commission Income	17,924	13,482	17,823	14,701
Other Operating Income	121,736	43,197	54,251	43,341
Total Operating Income	689,355	560,068	611,390	604,519
Impairment Gain/(Loss) or Loans and Receivables	(85,057)	(43,430)	(26,188)	(86,327)
Net Operating Income	604,298	516,638	585,202	518,192
Less: Operating Expenses				
Personnel Expenses	194,514	150,124	172,665	129,343
Depreciation of Property, Plant & Equipment	15,848	20,775	17,975	20,775
Amortisation of Intangible Assets	1,118	812	1312	812
Amortisation of Leasehold Property	117	117	117	117
Defined Benefit Plans	6,715	6,711	6,711	6,711
Other Operating Expenses	178,754	130,535	177,938	165,604
Total Operating Expenses	397,066	309,074	376,718	323,362
Operating Profit/(Loss) Before Value Added Tax and NBT on Financial Services	207,232	207,564	208,484	194,830
Value Added Tax & NBT on Financial Services	(47,245)	(22,223)	(39,713)	(37,980)
Operating Profit/(Loss) After Value Added Tax and NBT on Financial Services	159,987	185,341	168,771	156,850
Add: Share of Associate Company's Profit Before Taxation	(1,577)	6,034	44,804	29,235
Profit Before Taxation from Operations	158,410	191,375	213,575	186,085
Income Tax Expenses	(39,680)	(42,853)	(59,213)	(55,350)
Profit After Taxation	118,730	148,522	154,362	130,735
Earnings per Share	39.5	49.4	51.4	43.5
Dividend per Share	-	-	-	-

3rd Quarter		4th Quarter		Total	
Oct-Dec 16	Oct-Dec 15	Jan-Mar 17	Jan-Mar 16	Apr 16-Mar 17	Apr 15-Mar 16
Rs. 000	Rs. 000	Rs. 000	Rs. 000	Rs. 000	Rs. 000
1,356,264	1,147,257	1,429,401	1,129,835	5,286,060	4,301,828
(798,687)	(547,029)	(926,147)	(576,479)	(3,136,218)	(2,098,378)
557,577	600,228	503,254	553,356	2,149,842	2,203,450
18,954	15,064	28,921	15,680	83,622	58,927
18,954	15,064	28,921	15,680	83,622	58,927
33,609	30,640	66,255	22,343	275,851	139,520
610,140	645,932	598,430	591,379	2,509,315	2,401,897
(48,050)	29,900	(465,771)	(134,960)	(625,066)	(234,816)
562,090	675,832	132,659	456,419	1,884,249	2,167,081
174,908	132,926	107,818	96,180	649,905	508,573
19,182	19,093	12,927	(11,567)	65,932	49,076
4286	783	(3,930)	(1,957)	2,786	450
117	117	117	117	468	468
6,707	6,711	8,194	3,323	28,327	23,456
187,360	162,089	270,456	274,769	814,508	732,998
392,560	321,719	395,582	360,865	1,561,926	1,315,021
169,530	354,113	(262,923)	95,554	322,323	852,060
(44,010)	(65,849)	18,130	(15,038)	(112,838)	(141,090)
125,520	288,264	(244,793)	80,516	209,485	710,970
16,886	14,418	44,081	41,988	104,194	91,675
142,406	302,682	(200,712)	122,504	313,679	802,645
(51,655)	(104,964)	38,883	(94,459)	(111,665)	(297,626)
90,751	197,718	(161,829)	28,045	202,014	505,019
30.2	65.8	(53.8)	9.3	67.2	168.0
-	7.0	-	-	-	7.0

Quarterly Analysis

Statement of Financial Position

	1st Quarter		2nd Quarter	
	Apr-Jun 16	Apr-Jun 15	July-Sep 16	July-Sep 15
	Rs. 000	Rs. 000	Rs. 000	Rs. 000
Assets				
Cash & Short Term Funds	429,363	562,028	452,733	297,269
Placement with other banks	474,330	445,396	265,461	451,489
Financial Investments-Available for Sale	6,620,965	5,118,884	6,929,068	5,344,772
Loan and Advances	8,717,885	6,815,568	9,625,786	6,895,667
Lease receivable	10,650,529	6,497,441	10,797,628	7,892,166
Hire Purchase receivable	6,681,639	7,304,058	6,447,112	7,217,968
Other Financial Assets	137,318	102,996	135,848	105,662
Inventories	31,158	16,080	27,773	14,918
Other Assets	83,581	61,767	77,224	47,892
Current tax receivable	-	-	-	-
Investment in Associates	922,004	800,415	977,179	829,650
Investments Properties	442,055	198,769	174,184	213,769
Property, Plant & Equipment	1,808,322	1,741,623	1,812,087	1,742,079
Leasehold Property	42,491	42,960	42,374	57,823
Intangible Assets	13,170	2,428	11,431	4,675
Total Assets	37,054,812	29,710,414	37,775,887	31,115,799
Liabilities				
Bank overdraft	303,635	179,092	319,988	306,658
Deposits due to customers	16,055,008	14,173,597	16,128,498	14,815,010
Debt instruments issued and other borrowings	11,876,679	6,534,293	11,975,334	6,848,456
Other Financial Liabilities	504,204	633,527	579,382	660,551
Current tax liabilities	2,241	56,346	48,560	(3,692)
Deferred tax liabilities	343,259	214,646	343,259	238,578
Other liabilities	17,508	268	18,522	71
Retirement benefit obligations	151,589	126,144	157,362	121,824
Total Liabilities	29,254,124	21,917,912	29,570,905	22,987,455
Equity				
Stated capital	36,000	36,000	36,000	36,000
Revaluation reserve	1,535,877	1,482,934	1,546,249	1,482,934
Statutory reserve fund	631,400	581,400	631,400	581,400
General reserve	4,086,430	3,886,430	4,086,430	3,886,430
Investment Fund Reserve	-	-	-	-
Available for sale reserve	268,524	757,033	508,086	962,140
Retained earnings	1,242,457	1,048,705	1,396,817	1,179,440
Total Equity	7,800,688	7,792,502	8,204,982	8,128,344
Total Liabilities and Shareholders Equity	37,054,812	29,710,414	37,775,887	31,115,799
Net Assets Per Share	2,595	2,592	2,730	2,704

3rd Quarter		4th Quarter	
Oct-Dec 16	Oct-Dec 15	Jan-Mar 17	Jan-Mar 16
Rs. 000	Rs. 000	Rs. 000	Rs. 000
807,186	347,609	1,244,554	344,062
296,715	458,749	53,501	464,984
4,760,068	5,481,646	3,893,552	4,641,115
10,694,459	7,457,392	11,366,577	8,302,333
11,063,555	9,264,659	11,093,954	9,925,519
6,291,857	6,962,194	6,184,744	6,825,676
145,490	109,986	445,787	110,440
12,202	27,318	7,882	16,467
84,742	63,516	81,732	72,414
-	-	121,051	27,212
987,403	844,068	995,977	927,318
158,773	471,669	158,340	448,234
1,772,876	1,752,428	1,790,296	1,803,939
42,257	42,726	42,140	42,608
8,648	8,463	12,577	12,386
37,126,232	33,292,421	37,492,664	33,964,707
401,489	366,662	1,092,434	412,472
16,541,510	15,178,560	17,017,674	15,815,590
10,778,394	8,611,743	10,165,837	8,527,169
690,845	680,657	776,819	1,052,327
33,875	48,407	-	-
343,259	238,578	361,223	343,259
24,568	-	39,640	13,423
163,382	127,270	171,772	146,235
28,977,321	25,251,877	29,625,399	26,310,475
36,000	36,000	36,000	36,000
1,539,587	1,482,932	1,535,061	1,539,615
631,400	581,400	661,400	631,400
4,086,430	3,886,430	4,086,430	4,086,430
-	-	-	-
367,927	697,665	256,644	237,060
1,487,567	1,356,118	1,291,730	1,123,727
8,148,911	8,040,544	7,867,265	7,654,232
37,126,232	33,292,421	37,492,664	33,964,707
2,711	2,675	2,617	2,546

Glossary

A

Accounting Policies
The specific principles, bases, conventions, rules and practices adopted by an entity in preparing and presenting Financial Statements.

Accrual Basis
Recognising the effects of transactions and other events when they occur without waiting for receipt or payment of cash or its equivalents.

Amortisation
The systematic allocation of the depreciable amount of an asset over its useful life.

Amortised Cost
Amount at which the financial asset or 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 that initial amount and the maturity amount and minus any reduction for impairment.

Associate
An entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in joint venture.

Available-for-Sale
All assets not in any of the three categories, namely, held to maturity, Fair Value through Profit or Loss and Loans & Receivable. It is a residual category. It does not mean that the entity stands ready to sell these all the time.

C

Capital Adequacy ratios
The relationship between capital and the risk weighted assets as prescribed by the Central Bank of Sri Lanka developed by modifying International best practices on maintenance of Capital for financial Institutions, to suit the local requirements.

Collective Impairment Provisions
Impairment is measured on a collective basis for homogeneous groups of loans that are not considered individually significant.

Contingencies
A condition or situation existing at Balance Sheet date where the outcome will be confirmed only by occurrence or non-occurrence of one or more future events.

Corporate governance
The process by which Corporate Institutions are governed. It involves the way in which authority is exercised over the management and the direction of the Company, the supervisions of executive roles and the responsibility and accountability towards owners and other parties.

Cost Method
This is a method of accounting for an investment whereby the investment is initially recognised at cost. The investor recognises income from the investment only to the extent that the investor receives distribution from accumulated profits of the investee arising after the date of acquisition. Distributions received in excess of such profits are regarded as a recovery of investment and are recognised as a reduction of the cost of the investment.

Cost to Income ratio
Total operating expenses excluding impairment charge/(reversed)for loans and advances expressed as a percentage of operating Income.

Credit Rating
An evaluation of a corporate's ability to repay its obligations or the likelihood of not defaulting, carried out by an independent rating agency.

Credit Risk
Credit risk is the risk of financial loss to the Company if a customer or counter party to a financial instrument fails to meet its contractual obligations, and arises principally from the loans and advances to customers and banks and investment debt securities.

D

Debt to equity
Total Borrowings expressed as a percentage of equity.

Deferred Tax
Sum set aside in the financial statements for taxation that would become payable/receivable in a financial year other than the current financial year.

Derecognition
The removal of a previously recognised financial asset or financial liability from an entity's statement of financial position.

Dividend cover
Profit after tax divided by gross dividends. This ratio measures the number of times dividends is covered by the current year's distributable profits.

Dividend Yield
Dividend earned per share as a percentage of its market value.

E

Earnings per share
Net profit after tax and after dividend on Preference shares divided by the number of ordinary shares in issue.

Economic Value added
A measure to assess productivity of a business that takes into consideration cost of total invested equity.

Effective Income Tax Rate
Provision for taxation divided by the net profit before taxation.

Effective Interest Rate
Rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instruments or when appropriate a shorter period to the net carrying amount of the financial asset or financial liability.

Equity Method
This is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition changes in the investor's share of net assets of the investee. The profit or loss and other comprehensive income of the investor include the investor's share of the profit or loss and other comprehensive income of the investee.

F

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

Finance Lease
A contract whereby a lessor conveys to the lessee the right to use an asset for rent over an agreed period of time which is sufficient to amortise the capital outlay of the lessor. The lessor retains ownership of the asset but transfers substantially all the risks and rewards of ownership to the lessee.

Financial Instrument
A financial instrument is any contract that gives rise to both a financial asset in one entity and a financial liability or equity instrument in other entity.

I

Impairment
This occurs when recoverable amount of an asset is less than its carrying amount.

Impaired Loans
Loans where identified impairment provisions have been raised and also include loans which are collateralised or where indebtedness has already been written down to the expected realisable value. The impaired loan category may include loans, which, while impaired, are still performing.

Impairment allowances
Impairment allowances are a provision held as a result of the rising of a charge against profit for the incurred loss. An impairment allowance may either be identified or unidentified and individual (specific) or collective (portfolio).

Impairment Provision Cover
Total impairment provision expressed as a percentage of non-performing loans.

Individually Assessed Impairment
Exposure to loss is assessed on all individually significant accounts and all other accounts that do not qualify for collective assessment.

Intangible Asset
An Intangible Asset is an identifiable non-monetary asset without physical substance.

Interest Cover
Profits before interest and taxes divided by the interest cost. This ratio measures the number of times Interest is covered by the current year’s profits before interest and taxes.

K

Key Management Personnel (KMP)
Key management personnel are those persons having authority and responsibility for planning,directing and controlling the activities of the entity,directly or indirectly.

L

Liquid Assets
Assets that are held in cash or in a form that can be converted to cash readily, such as deposits with banks free from any charge or lien and Government securities.

Liquid Assets ratio
Assets that are held in cash or in a form that can be converted to cash readily (as prescribed by the Central Bank of Sri Lanka) divided by the total deposits and outstanding borrowings excluding secured borrowings and borrowings considered as capital funds.

Loans and Receivables
Conventional loan assets that are unquoted (originated).

Loss Given Default (LGD)
LGD is the percentage of an exposure that a lender expects to loss in the event of obligor default.

Loan to Value Ratio (LTV)
LTV ratio is a computation that expresses the amount of a first disbursement as a percentage of the total appraised value of assets kept as security.

M

Market Risk
This refers to the possibility of loss arising from changes in the value of a financial instrument as a result of changes in market variables such as interest rates, exchange rates, credit spreads and other asset prices.

Market Value Added (MVA)
The difference between the current market value of a firm and the capital contributed by investors. Market value added represents the wealth generated by a company for its shareholders since inception. Since the main goal of a for-profit organisation is to maximise shareholders' wealth, market value added is an important measure to analyse how much value a company has added to the wealth of its shareholders. Higher market value added indicates higher wealth generation.

Materiality
The relative significance of a transaction or an event, the omission or misstatement of which could influence the economic decisions of users of Financial Statements.

N

Net assets per share
Shareholders’ funds excluding preference shares divided by the number of ordinary shares in issue.

Net Interest Income (NII)
The difference between the amount a Financial Institution earns on assets such as Loans and securities and what it incurs on liabilities such as deposits and borrowings.

Net Interest Margin
Net interest income expressed as a percentage of average interest earning assets.

Non-performing Loans
A loan placed on a cash basis (i.e. Interest Income is only recognised when cash is actually collected) after when six instalments or more are overdue, as there is reasonable doubt regarding the collectability of its instalments of capital and interest.

Non Performing Ratio
Total non-performing loans expressed as a percentage of the total loans and advances.

O

Operational Risk
This refers to the risk of loss resulting from inadequate or failed internal processes, peoples and systems or from external events.

P

Price earnings ratio
Market price of an ordinary share divided by earnings per share.

R

Related parties
Parties where one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions.

Return on average assets
Net profit after tax divided by the average assets.

Return on shareholders’ funds
Net profit after tax divided by the shareholders’ funds.

Risk Weighted Assets
On-Balance Sheet assets and the credit equivalent of off-Balance Sheet assets multiplied by the relevant risk weighting factors prescribed by the Central Bank of Sri Lanka.

S

Segmental Analysis
Analysis of financial information by segments of an organisation specifically, the different Industries and the different business lines in which it operates.

Shareholders’ funds
Total of stated capital plus capital and revenue reserves.

Sustainability report
Sustainability reporting is a practice of measuring, disclosing, and being accountable for organisational performance while working towards the goal of sustainable development. A sustainability report provides a balanced and reasonable representation of the sustainability performance of the reporting organisation.

T

Tier I capital
Core capital representing permanent shareholders’ equity and reserves created or increased by appropriations of retained earnings or other surpluses.

Tier 11 Capital
Supplementary capital that consist of revaluation reserves, general provisions and debt instruments such as subordinated term debts and other hybrid capital instruments that combine characteristics of equity and debt.

V

Value added
Value of wealth created by providing financial and other related services less the cost of providing such services.

Basis of Ratios

Attrition rate (%) = $\frac{\text{Number of Employees resigned during the year}}{\text{Number of Employees}}$ X 100

Carbon Footprint Intensity (Per employee) = $\frac{\text{Total Carbon Emissions}}{\text{Number of Employees}}$

Cost to income ratio (%) = $\frac{\text{Total operating cost with VAT on financial Services}}{\text{Total operating income}}$ X 100

Debt to equity ratio (Times) = $\frac{\text{Borrowings}}{\text{Equity}}$

Dividend Cover (Times) = $\frac{\text{Profit /loss attributable to ordinary shareholders}}{\text{Total dividends}}$

Dividend Payout (%) = $\frac{\text{Total dividends}}{\text{Profit/loss attributable to ordinary shareholders}}$ X 100

Dividend Yield (%) = $\frac{\text{Dividend per ordinary share}}{\text{Market Price per share}}$ X 100

Earnings per share (EPS) (Rs.) = $\frac{\text{Profit/loss attributable to ordinary shareholders}}{\text{Number of shares}}$

Equity asset ratio (%) = $\frac{\text{Equity}}{\text{Total Assets}}$ X 100

Gross non-performing advances ratio (%) = $\frac{\text{Non-performing portfolio (net of unearned income)}}{\text{Gross portfolio (net of unearned income)}}$ X 100

Interest cover (Times) = $\frac{\text{Profit before interest and tax}}{\text{Interest cost}}$

Interest Spread (%) = Yield on average interest earning assets - Cost on average interest bearing liabilities

Local hiring of employees (%) = $\frac{\text{Locally hired employees}}{\text{Total number of employees}}$ X 100

Market Capitalisation (Rs.) = Market price per share X Number of shares

Net assets per share (Rs.) = $\frac{\text{Total shareholders' Funds}}{\text{Number of shares}}$

Net interest margin (%) = $\frac{\text{Net interest income}}{\text{Average interest earning assets}}$ X 100

Operating Profit margin (%) = $\frac{\text{Operating profit after VAT on financial services}}{\text{Gross Income}}$ X 100

Price earning (PE) (Times) = $\frac{\text{Market price per share}}{\text{Earnings per share}}$

Price to book Value (PVB) (Times) = $\frac{\text{Market price}}{\text{Net assets per share}}$

Provision cover (Times) = $\frac{\text{Cumulative impairment}}{\text{Non-performing loans and advances}}$

Return on asset (ROA) (%) = $\frac{\text{Profit after tax}}{\text{Total Average assets}}$ X 100

Return on shareholder's Funds (Equity) = $\frac{\text{Profit after tax}}{\text{Equity}}$ X 100

Training hours per employee (hrs) = $\frac{\text{Total Training hours}}{\text{Number of employees}}$

Value added per employee (Rs.) = $\frac{\text{Economic value generated}}{\text{Number of employees}}$

Corporate Information

Name of the Company

Mercantile Investments and Finance PLC

Legal Form

Public Limited Liability Company incorporated in Sri Lanka under the Companies Ordinance No 51 of 1938 and re-registered under the Companies Act No. 07 of 2007. A licensed finance company under the Finance Business Act No 42 of 2011.

Company Registration Number

PB 76 PQ

Tax Payer Identification Number

104021794

VAT Registration Number

104021794 7000

Registered Office

No. 236 Galle Road,
Colombo 3

Head Office

No. 236 Galle Road, Colombo 3
Telephone: 2343720 – 7
Fax: 2434524
Email:mercantile@mi.com.lk
Website: http// www.mi.com.lk

Board of Directors

Saroja Hemakumar Jayawickrama Weerasuriya *(Chairman)*
Gerard George Ondaatjie *(Managing Director)*
Pathiranage Mahes Amarasekera *(Deputy Managing Director)*
Shermal Hemaka Jayasuriya *(Finance Director)*
Angeline Myrese Ondaatjie
Travice John Ondaatjie
Punyakanthi Tikiri Kumari Navaratne
Nawagamuwage Hasantha Viraj Perera
Singappuli Mudiyanselage Susantha Sanjaya Bandara
Pathmanathan Cumarasamy Guhashanka

Company Secretary

Sonali Pethiyagoda

Audit Committee

Singappuli Mudiyanselage Susantha Sanjaya Bandara - *(Chairman of the Committee)*
Saroja Hemakumar Jayawickrama Weerasuriya
Nawagamuwage Hasantha Viraj Perera

Sonali Pethiyagoda - Company Secretary
- *(Secretary to the Committee)*

Credit Committee

Gerard George Ondaatjie - *(Chairman of the Committee)*
Pathiranage Mahes Amarasekera
Shermal Hemaka Jayasuriya

Dhanushka Fonseka -Director (non-board) –Credit & Marketing - *(Secretary to the Committee)*

Remuneration Committee

Saroja Hemakumar Jayawickrama Weerasuriya
- *(Chairman of the Committee)*
Nawagamuwage Hasantha Viraj Perera
Punyakanthi Tikiri kumari Navaratne

Sonali Pethiyagoda-Company Secretary
- *(Secretary to the Committee)*

Nominations Committee

Saroja Hemakumar Jayawickrama Weerasuriya
- *(Chairman of the Committee)*
Gerard George Ondaatjie
Singappuli Mudiyanselage Susantha Sanjaya Bandara
Nawagamuwage Hasantha Viraj Perera

Sonali Pethiyagoda-Company Secretary
- *(Secretary to the Committee)*

Integrated Risk Management Committee

Nawagamuwage Hasantha Viraj Perera
- *(Chairman of the Committee)*
Gerard George Ondaatjie
Pathiranage Mahes Amarasekera
Shermal Hemaka Jayasuriya

Shehan Sandanayaka – Manager – Risk & Compliance
- *(Secretary to the Committee)*

Assets & Liability Committee

Gerard George Ondaatjie (*Chairman of the committee)*
Pathiranage Mahes Amarasekera (Deputy Managing Director)
Shermal Hemaka Jayasuriya (Finance Director)
Corporate Management
Shehan Sandanayaka – Manager – Risk & Compliance - *(Secretary to the Committee)*

Related Party Transaction Review Committee

Singappuli Mudiyanselage Susantha Sanjaya Bandara
- *(Chairman of the Committee)*
Saroja Hemakumar Jayawickrama Weerasuriya
Shermal Hemaka Jayasuriya (Finance Director)
Nawagamuwage Hasantha Viraj Perera

Sonali Pethiyagoda-Company Secretary
- *(Secretary to the Committee)*

External Auditors

BDO Partners
Chartered Accountants

Internal Auditors

Ernst & Young
Chartered Accountants

Bankers

Commercial Bank of Ceylon PLC
Hatton National Bank PLC
Seylan Bank PLC
Sampath Bank PLC
NDB Bank PLC
Nations Trust Bank PLC
HSBC Ltd
Peoples Bank
Bank of Ceylon
Union Bank Plc.
PanAsia Bank Plc.
Cargills Bank PLC

Credit Rating

Long-term Financial Institution Rating at BBB-(lka) (stable outlook) by Fitch Ratings.

Notice of Meeting

NOTICE IS HEREBY given that the Fifty-fourth (54) Annual General Meeting of MERCANTILE INVESTMENTS AND FINANCE PLC will be held at No 236, Galle Road, Colombo 3, on 20th October 2017, at 11.00 a.m. for the following purposes:

- To receive and consider the Report of Directors and the Statement of Accounts for the year ended 31st March 2017 and the Report of the Auditors thereon.
- To re-elect Directors retiring by rotation in terms of Article 23 (7) of the Articles of Association.
- To appoint Messrs. Ernst & Young, Chartered Accountants as Auditors of the Company for the year 2017/18 and to authorise the Directors to determine their remuneration.
- To authorise the Board of Directors to determine donations.

By Order of the Board,

Ms. Sonali Pethiyagoda
Company Secretary

Colombo
14th September 2017

Notes

1. A member who is entitled to attend and vote at the above- mentioned meeting is entitled to appoint a proxy, who need not also be a member to attend instead of him/her.
2. A Form of proxy is enclosed in the report.
3. The completed Proxy Form should be deposited at the Registered Office of the Company at No 236, Galle Road, Colombo 3, not less than 48 hours before the time fixed for holding the meeting.

Form of Proxy

I/We*.. of

....

being a member/members* of MERCANTILE INVESTMENTS AND FINANCE PLC, do hereby appoint; ....

.... of...or failing him/her

Mr. Saroja Hemakumar Jayawickrema Weerasuriya or failing him
Mr. Gerard George Ondaatjie or failing him
Mr. Pathiranage Mahes Amarasekara or failing him
Mr. Shermal Hemaka Jayasuriya or failing him
Ms. Angeline Myrese Ondaatjie or failing her
Mr. Travice John Ondaatjie or failing him
Ms. Punyakanthi Tikiri Kumari Navaratne or failing her
Mr. Nawagamuwage Hasantha Viraj Perera or failing him
Mr. Singappuli Mudiyanselage Susantha Sanjaya Bandara or failing him
Mr. Pathmanathan Cumarasamy Guhashanka

as my/our* proxy to represent me/us* and to vote for me/us* on my/our* behalf at the Annual General Meeting of the Company to be held on 20th October 2017 at 11.00 a.m. at No. 236, Galle Road, Colombo 03 and at any adjournment thereof and at every poll which may be taken in consequence thereof.

		FOR	AGAINST
1)	To receive and adopt the Report of Directors and the Statement of Accounts for the year ended 31st March 2017, with the Report of the Auditors there on.	☐	☐
2)	To elect Mr. P M Amarasekara retiring in terms of Article 23(7) of the Articles of Association of the Company.	☐	☐
3)	To elect Ms. A M Ondaatjie retiring in terms of Article 23(7) of the Articles of Association of the Company.	☐	☐
4)	To elect Mr. T J Ondaatjie retiring in terms of Article 23(7) of the Articles of Association of the Company.	☐	☐
5)	To appoint Messrs. Ernst & Young, as Auditors and authorise Directors to determine their remuneration.	☐	☐
6)	To authorise the Directors to determine contributions for charities and other donations for the year 2017/18.	☐	☐

As witness my/our* hand this ....day of ....2017.

....
Signature of Shareholder/s

Note: Please delete the inappropriate words.

INSTRUCTIONS AS TO COMPLETION

1. Kindly perfect the Form of Proxy, after filling in legibly your full name and address by signing in the space provided and please fill in the date of signature.
2. If the Proxy Form is signed by an Attorney, the relative Power of the Attorney should also accompany the Proxy Form for registration, if such Power of Attorney has not already been registered with the Company.
3. In the case of a Company/Corporation, the proxy must be under its Common Seal which should be affixed and attested in the manner prescribed by its Articles of Association.
4. The completed Form of Proxy should be deposited at the registered office of the Company at No. 236, Galle Road, Colombo 3, not less than 48 hours before the time of the meeting.

Voting at Meetings of Shareholders

Article 14 of the Articles of Association of the Company, dealing with voting is quoted below, for information of shareholders:

Voting at Meetings of Shareholders

1. In the case of a meeting of shareholders unless a poll is demanded, voting at the meeting shall be by whichever of the following methods as determined by Chairperson of the meeting:
    (a) Voting by voice; or
    (b) Voting by show of hands.
2. A declaration by the chairperson of the meeting that a resolution is carried by the requisite majority is conclusive evidence of that fact, unless a poll is demanded in accordance with Article 14(3).
3. At a meeting of shareholders, a poll may be demanded by-
    (a) Not less than three (3) shareholders having the right to vote at the meeting; or
    (b) A shareholder or shareholders representing not less than ten per centum of the total voting rights of all shareholders having the right to vote at the meeting.
4. A poll may be demanded either before or immediately after the vote is taken on a resolution.
5. If a poll is taken, votes must be counted according to the votes attached to the shares of each shareholder present and voting.
6. The Chairperson of a shareholder's meeting is not entitled to a casting vote.
7. If a poll is duly demanded (and the demand be not withdrawn) it shall be taken in such manner (including the use of ballot or voting papers or tickets) as the person presiding at the meeting may direct and the result of a poll shall be deemed to be the resolution of the meeting at which the poll was demanded. The person presiding may (and if so requested shall) appoint a scrutiniser and may adjourn the meeting to some place and time fixed by him for the purpose of taking and declaring the result of the poll.
8. The demand for a poll shall not prevent the continuance of a meeting for the transaction of any business other than the question on which the poll has been demanded.
9. No objection shall be made to the validity of any vote except at the meeting or poll at which such vote shall be tendered and every vote to which no objection shall be made at such meeting or poll shall be deemed valid for all purposes of such meeting or poll whatsoever.

Stakeholder Feedback Form

For purpose of submitting a comment or query, please complete the following and return this page to:

Finance Director,
Mercantile Investments and Finance PLC,
No. 236, Galle Road,
Colombo 03.

Details of party submitting comment or query –

Name *(Individual/Corporate)*	
Permanent Mailing Address	
Contact Number	
E-mail	
Stakeholder Category ***(Investor/Customer/Supplier/ General Public/Other)***	

Comment or query :

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