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## INDEPENDENT AUDITOR'S REPORT

### TO THE SHAREHOLDERS OF MERCANTILE INVESTMENTS & FINANCE PLC

#### Report on the audit of the Financial Statements

We have audited the financial statements of Mercantile Investments & Finance PLC ("The Company"), which comprise the statement of financial position as at 31 March 2020, and the statement of profit or loss and statement of comprehensive income, statement of changes in equity and, cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements of the Company give a true and fair view of the financial position of the Company as at 31 March 2020, and of its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

#### Basis for opinion

We conducted our audit in accordance with Sri Lanka Auditing Standards (SLAuSs). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Company in accordance with the Code of Ethics issued by CA Sri Lanka (Code of Ethics) and we have fulfilled our other ethical responsibilities in accordance with the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### Key audit matters

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

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

| Key Audit Matter | How our audit addressed the matter |
|------------------|------------------------------------|
|------------------|------------------------------------|

#### Impairment allowance for Loans & receivables, Lease receivable & Hire Purchase receivables

We considered the impairment allowance for Loans & receivables, Lease receivable & Hire Purchase receivables as a key audit matter. Significant judgments and assumptions were used by the management to determine the impairment allowance and complex calculations were involved in its estimation. Probable impacts of COVID -19 outbreak on the economically impacted customers and related government relief measures on the key assumptions, the higher level of estimation uncertainty involved, and materiality of the amounts reported in the Company's financial statements, underpinned our basis for considering it as a Key Audit Matter.

As at 31 March 2020, Loans & receivables, Lease receivable & Hire Purchase receivables net of impairment amounted to Rs.33 Bn. These collectively contributed 76% to the Company's total assets.

The Note 10 of the financial statements describes the basis of impairment allowance and assumptions used by the management in its calculation.

#### Revaluation of Land & Buildings:

As of 31 March 2020, the Company carried freehold land and buildings at fair value amounting to Rs.1.7 Bn and Rs 512 Mn respectively, of which Rs.301 million has been recognized through OCI.

Fair value was determined by an external valuer engaged by the Company. The valuation was significant to our audit due to the use of estimates in the valuation techniques, and valuation is judgmental and is based on certain key assumptions. Given the significance of assumptions associated with the valuation of these assets we have considered the valuation of freehold land and building as a key audit matter.

Refer note 31.4 to the financial statements for significant accounting judgements, estimates and assumptions related to valuation of freehold land and buildings.

#### Management's use of significant judgements relating to the impacts of the evolving COVID-19 pandemic on the Company

Management has assessed the impact of the evolving COVID-19 pandemic on its business and financial statements of the Company as disclosed in Note (refer to COVID-19 impact note 53)

We considered such management's assessment in the wake of the evolving COVID-19 pandemic as a key audit matter, since it involved the use of significant management judgements and estimates considering future events, circumstances and impacts on cash flows, based on available information.

The nature of the significant assumptions involved, are disclosed in Note (refer to COVID-19 impact note 53) to the financial statements.

#### Other information included in the 2020 Annual Report

Management is responsible for the other information. The other information comprises the Company's 2020 annual report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we will not express any form of assurance conclusion thereon. In connection with our audit of the financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

#### Responsibilities of management and those charged with governance for the financial statements

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

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

Those charged with governance are responsible for overseeing the Company's financial reporting process.

#### Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SLAuSs will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with SLAuSs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

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

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

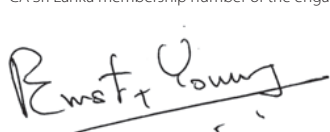
We also provide those charged with governance with a statement that we have complied with ethical requirements in accordance with the Code of Ethics regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

#### Report on Other Legal and Regulatory Requirements

As required by section 163 (2) of the Companies Act No. 07 of 2007, 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.

CA Sri Lanka membership number of the engagement partner responsible for signing this independent auditor's report is 2440.



26<sup>th</sup> June 2020  
Colombo

Partners: W. R. H. Fernando FCA FCMA | R. N. de Saram ACA FCMA | Ms. N. A. De Silva FCA | Ms. Y. A. De Silva FCA | W. R. H. De Silva ACA ACMA  
W.K. B. S. P. Fernando FCA FCMA | Ms. K. R. M. Fernando FCA ACMA | Ms. L. K. H. L. Fonseka FCA | A. P. A. Gunasekara FCA FCMA | A. Herath FCA |  
D. K. Hulugamuwa FCA FCMA LLB (Lond.) | H. M. A. Jayasinghe FCA FCMA | Ms. A. A. Ludowyke FCA FCMA | Ms. G. G. S. Manatunga FCA |  
Ms. P.V. K. N. Sajeewani FCA | N. M. Sulaiman ACA ACMA | B. E. Wijesuriya FCA FCMA  
Principal: G. B. Goudian ACMA | A. A. J. R. Perera ACA ACMA | T. P. M. Ruberu FCMA FCCA  
A member firm of Ernst & Young Global Limited

## STATEMENT OF COMPREHENSIVE INCOME

| For the year ended 31 <sup>st</sup> March  | 2020<br>Rs. '000   | 2019<br>Rs. '000   |
|--|--------------------|--------------------|
| <b>Gross income</b>  | <b>7,610,170</b>   | <b>7,638,497</b>   |
| Interest income  | 7,475,320          | 7,436,054          |
| Interest expenses  | (3,842,380)        | (3,861,878)        |
| <b>Net interest income</b>   | <b>3,632,941</b>   | <b>3,574,176</b>   |
| Fee and commission income  | 82,943             | 94,955             |
| <b>Net Fee and Commission Income</b>   | <b>82,943</b>      | <b>94,955</b>      |
| Other operating income   | 51,906             | 107,488            |
| <b>Total Operating Income</b>  | <b>3,767,790</b>   | <b>3,776,619</b>   |
| Impairment charge/(reversal) for loans and receivables and equity investments                                    | (484,009)          | (681,648)          |
| <b>Net Operating Income</b>  | <b>3,283,780</b>   | <b>3,094,971</b>   |
| <b>Less: Operating Expenses</b>  |                    |                    |
| Personnel expenses   | (989,859)          | (923,352)          |
| Depreciation and amortization  | (144,478)          | (99,494)           |
| Other operating expenses   | (1,013,253)        | (962,135)          |
| <b>Total operating expenses</b>  | <b>(2,147,590)</b> | <b>(1,984,982)</b> |
| <b>Operating Profit /(Loss) Before Value Added Tax, DRL and NBT on Financial Services</b>                        | <b>1,136,190</b>   | <b>1,109,988</b>   |
| Value Added Tax, NBT & DRL on financial services   | (460,859)          | (403,059)          |
| <b>Operating Profit /(Loss) After Value Added Tax, DRL and NBT on Financial Services</b>                         | <b>675,331</b>     | <b>706,929</b>     |
| Add: Share of associate company's profit   | 16,459             | 79,724             |
| <b>Profit Before Taxation from operations</b>  | <b>691,791</b>     | <b>786,653</b>     |
| <b>Less: Income tax expenses</b>   | <b>(320,082)</b>   | <b>(328,580)</b>   |
| <b>Profit for the year</b>   | <b>371,708</b>     | <b>458,073</b>     |
| <b>Other comprehensive Income/ (Expenses)</b>  |                    |                    |
| <b>Other Comprehensive Income/ (Expenses) to be reclassified to profit or loss in subsequent periods</b>         |                    |                    |
| Changes in fair value of financial investments through OCI   | -                  | -                  |
| <b>Other Comprehensive Income/ (Expenses) to be reclassified to profit or loss in subsequent periods</b>         | <b>-</b>           | <b>-</b>           |
| <b>Other Comprehensive Income/ (Expenses) not to be reclassified to profit or loss in subsequent periods</b>     |                    |                    |
| Changes in fair value of financial investments through OCI   | (251,709)          | (276,015)          |
| Net change in revaluation surplus  | 301,201            | -                  |
| Differed tax effect on revaluations surplus on Land & Building   | (84,336)           | -                  |
| Share of other comprehensive income of associates (net of tax)   | (15,815)           | 196,285            |
| Actuarial gain/(loss) on retirement benefit obligation   | 22,339             | (24,304)           |
| Differed tax effect on Actuarial Gain  | (13,104)           | 10,752             |
| <b>Net Other Comprehensive Income/ (Expenses) not to be reclassified to profit or loss in subsequent periods</b> | <b>(41,423)</b>    | <b>(93,282)</b>    |
| <b>Other Comprehensive Income/ (Expenses) for the year (net of tax)</b>  | <b>(41,423)</b>    | <b>(93,282)</b>    |
| <b>Total comprehensive income/ (Expenses) for the year (net of tax)</b>  | <b>330,285</b>     | <b>364,791</b>     |
| <b>Earnings Per Share</b>  |                    |                    |
| Basic earnings per share (Rs.)   | 123.66             | 152.39             |
| Diluted earnings per share (Rs.)   | 123.66             | 152.39             |
| Dividend per ordinary Share (Rs.)  | 20.00              | -                  |

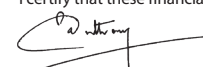
Figures in brackets indicate deductions.

## STATEMENT OF FINANCIAL POSITION

| As at 31 <sup>st</sup> March                                   | 2020<br>Rs. '000  | 2019<br>Rs. '000  |
|--|-------------------|-------------------|
| <b>Assets</b>  |                   |                   |
| Cash and cash equivalents                                      | 1,813,985         | 1,196,226         |
| Placement with banks at Amortized cost                         | 282,359           | 241,376           |
| Financial investments - at Fair Value through OCI              | 2,682,898         | 2,863,058         |
| Loans and receivables at Amortized Cost                        | 17,407,591        | 15,913,287        |
| Finance leases receivables at Amortized Cost                   | 13,746,155        | 12,722,875        |
| Hire purchase receivables at Amortized Cost                    | 1,605,426         | 3,308,315         |
| Financial investments - at Fair Value through OCI (unquoted)   | 70,427            | 70,427            |
| Other financial assets   | 438,638           | 499,594           |
| Inventories  | 9,540             | 23,231            |
| Other assets   | 45,984            | 96,740            |
| Current tax refunds  | 146,042           | -                 |
| Investment in associates                                       | 1,260,144         | 1,267,430         |
| Investment property  | 246,166           | 198,431           |
| Property, plant and equipment                                  | 3,105,781         | 2,848,159         |
| Right-of-use assets  | 223,255           | -                 |
| Leasehold property   | 40,739            | 41,207            |
| Intangible assets  | 45,987            | 64,211            |
| <b>Total Assets</b>  | <b>43,171,119</b> | <b>41,354,567</b> |
| <b>Liabilities</b>   |                   |                   |
| Bank overdraft   | 86,567            | 186,276           |
| Deposits due to customers at Amortized Cost                    | 22,814,923        | 21,176,433        |
| Debt instruments issued and other borrowings at Amortized Cost | 9,128,983         | 8,957,478         |
| Other financial liabilities                                    | 855,247           | 955,246           |
| Current tax liabilities  | -                 | 290,338           |
| Deferred tax liabilities                                       | 807,835           | 830,950           |
| Other liabilities  | 54,859            | 46,870            |
| Retirement benefit obligations                                 | 254,385           | 238,112           |
| Lease Liability  | 269,986           | -                 |
| <b>Total liabilities</b>                                       | <b>34,272,786</b> | <b>32,681,703</b> |
| <b>Shareholders' funds</b>                                     |                   |                   |
| Stated capital   | 36,000            | 36,000            |
| Revaluation reserve  | 2,325,585         | 2,124,535         |
| Statutory reserve fund   | 761,400           | 736,400           |
| General reserves   | 4,086,430         | 4,086,430         |
| Retained earnings  | 2,016,150         | 1,765,028         |
| Fair Value through OCI reserve                                 | (327,238)         | (75,529)          |
| <b>Total shareholders' funds</b>                               | <b>8,898,327</b>  | <b>8,672,864</b>  |
| <b>Total liabilities and shareholders' funds</b>               | <b>43,171,119</b> | <b>41,354,567</b> |
| <b>Net assets per share (Rs.)</b>                              | <b>2,960</b>      | <b>2,885</b>      |

#### Certification


I certify that these financial statements have been prepared in compliance with the requirements of the Companies Act No. 07 of 2007.



Deva Anthony  
Chief Financial Officer

The Board of Directors is responsible for these Financial Statements.

The financial statements were authorised for issue by the directors on 26<sup>th</sup> June 2020. The directors have the power to amend and reissue the financial statements. Signed for and on behalf of the Board by:



Gerard G. Ondaatje  
Managing Director  
26<sup>th</sup> June 2020  
Colombo



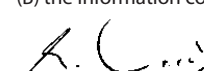
Sermal H. Jayasuriya  
Finance Director

## SELECTED PERFORMANCE INDICATORS

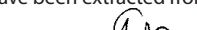
| As at 31 <sup>st</sup> March  | 2020      | 2019      |
|---|-----------|-----------|
| <b>Regulatory Capital Adequacy</b>  |           |           |
| Core Capital (Tier 1 Capital), Rs '000  | 5,944,032 | 6,467,552 |
| Total Capital Base, Rs '000   | 6,682,681 | 7,203,938 |
| Core capital adequacy ratio as % of risk weighted assets (Minimum 2020 - 6.5% / 2019 - 6%)    | 13.56%    | 14.98%    |
| Total capital adequacy ratio as % of risk weighted assets (Minimum 2020 - 10.5% / 2019 - 10%) | 15.25%    | 16.69%    |
| Capital funds to total deposits liability ratio (Minimum requirement, 10%)                    | 37.98%    | 40.96%    |
| <b>Asset Quality (Quality of Loan Portfolio)</b>  |           |           |
| Gross Non-Performing accommodations, Rs. '000   | 4,152,962 | 3,290,483 |
| Gross Non-Performing accommodations Ratio, %  | 11.69     | 9.62      |
| Net Non-Performing Accommodations Ratio, %  | 3.22      | 2.99      |
| <b>Profitability (%)</b>  |           |           |
| Interest Margin   | 9.85      | 10.04     |
| Return on assets (before Tax)   | 2.07      | 2.44      |
| Return on equity (after Tax)  | 4.18      | 5.28      |
| <b>Regulatory Liquidity (Rs. '000)</b>  |           |           |
| Required minimum amount of liquid assets  | 1,378,630 | 2,121,837 |
| Available amount of liquid assets   | 3,725,730 | 3,129,049 |
| Required minimum amount of Government securities  | 1,043,805 | 1,485,822 |
| Available amount of Government securities   | 1,697,557 | 1,691,903 |
| <b>Memorandum Information</b>   |           |           |
| Number of employees   | 1115      | 1040      |
| Number of branches  | 39        | 32        |
| Number of service centers   | -         | 7         |

#### Certification

We, the undersigned, being the Managing Director and the Finance Director of Mercantile Investments and Finance PLC certify jointly that:  
(A) the above statements have been prepared in compliance with the format and definitions prescribed by the Central Bank of Sri Lanka;  
(B) the information contained in these statements have been extracted from the audited financial statements of the company.



Gerard G. Ondaatje  
Managing Director  
26<sup>th</sup> June 2020  
Colombo



Sermal H. Jayasuriya  
Finance Director