



Mercantile Investments and Finance PLC

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INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF MERCANTILE INVESTMENTS AND FINANCE PLC

Report on the audit of the Financial Statements

We have audited the financial statements of Mercantile Investments and Finance PLC (The Company), which comprise the statement of financial position as at 31 March 2021, 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 2021, 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 matters specific to Company

Key Audit Matter

Impairment allowance for loans & receivables and lease rentals receivable & hire purchase.

As described in Note(s) 23 to 25, impairment allowance on such financial assets carried at amortised cost is determined in accordance with Sri Lanka Accounting Standard - SLFRS 9 Financial Instruments

This was a key audit matter due to:

- materiality of the reported impairment allowance which involved complex calculations; and
- the degree of assumptions, judgements and estimation uncertainty associated with the calculations

Key areas of significant judgements, estimates and assumptions used by management in the assessment of the impairment allowance included the following:

- the probable impacts of COVID-19 and related industry responses (e.g. government stimulus packages and debt moratorium relief measures granted by the Company); and
- forward-looking macroeconomic factors, including developing and incorporating macroeconomic scenarios, given the wide range of potential economic outcomes and probable impacts from COVID-19 that may impact future expected credit losses.

IT systems and controls relevant to financial reporting

The Company uses multiple IT systems in its operations. We selected IT systems and controls relevant to financial reporting as a key audit matter due to:

- The Company's financial reporting process being heavily dependent on information derived from its IT systems and
- Key financial statement disclosures involving the use of multiple system-generated reports and calculations thereon
- A changed working environment of increased remote access

Impact of moratoriums and other relief measures on recognition of interest income

Moratoriums and other relief measures were granted by the Company to customers affected by the COVID - 19 Pandemic.

Impact of moratoriums and other relief measures on the recognition of interest income on loans & receivables, lease rentals receivable & hire purchase was a key audit matter due to:

- Significant judgments that were applied in determining whether such moratoriums and other relief measures have resulted in substantial modifications or not, to contracts with customers as set out in Note 3.2 (ii) to the financial statements
- Use of various calculations by management to quantify the impacts of such moratoriums and other relief measures on the amount of revenue recognized for the period

Other information included in the 2021 Annual Report

Other information consists of the information included in the Annual Report, other than the financial statements and our auditor's report thereon. Management is responsible for the other information.

Our opinion on the financial statements does not cover the other information and we do 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 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. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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.

07 June 2021
Colombo

Partners: W R H Fernando FCA FCM, R N de Sarum ACA FCM, M S A De Silva FCA, M S Y De Silva FCA, W R De Silva ACA FCM, W R S P Fernando FCA FCM, M S K S M Fernando FCA FCM, M S L K H L Fonseka FCA, A P A Gunasekera FCA FCM, A Herath FCA, D K Hiralagimulla FCA FCM, L B (Lomb) H M A Jayasinghe FCA FCM, M A A Ludowyke FCA FCM, M S G S Manatunga FCA, A J R Perera ACA FCM, M S P K N Sajjanani FCA, N M Sutarani ACA FCM, B E Wijesuriya FCA FCM

Principals: G B Goudan ACA, T P M Ruberu FCA FCM

A member firm of Ernst & Young Global Limited

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31st March	2021 Rs. '000	2020 Rs. '000
Gross income	6,496,631	7,610,170
Interest income	6,273,624	7,475,320
Interest expenses	(3,219,671)	(3,842,380)
Net interest income	3,053,953	3,632,940
Fee and commission income	74,378	82,943
Net fee and commission income	74,378	82,943
Other operating income	148,630	51,906
Total operating income	3,276,961	3,767,789
Impairment (charge)/reversal for loans and receivables and other financial assets	(42,134)	(484,009)
Net operating income	3,234,827	3,283,780
Less: Operating expenses		
Personnel expenses	(988,823)	(989,859)
Depreciation of PPE and Right-of-use assets and amortization of intangible assets	(136,725)	(144,478)
Other operating expenses	(956,702)	(1,013,253)
Total operating expenses	(2,082,250)	(2,147,590)
Operating profit before VAT, NBT and DRL on financial services	1,152,577	1,136,190
Value Added Tax, NBT & DRL on financial services	(288,422)	(460,859)
Operating profit after VAT, NBT and DRL on financial services	864,155	675,331
Add: Share of associate company's profit / (Loss) net of tax	(36,654)	16,459
Profit before taxation from operations	827,501	691,790
Less: Income tax expenses	(213,358)	(320,082)
Profit for the year	614,143	371,708
Other comprehensive income/(expenses)		
Other comprehensive income/(expenses) to be reclassified to profit or loss in subsequent periods		
Changes in fair value of financial investments through OCI	-	-
Other comprehensive income/(expenses) to be reclassified to profit or loss in subsequent periods		
Other comprehensive income/(expenses) not to be reclassified to profit or loss in subsequent periods		
Changes in fair value of financial investments through OCI	556,625	(251,709)
Net change in revaluation surplus on Land & Buildings	213,337	301,201
Deferred tax effect on revaluations surplus on Land & building	39,850	(84,336)
Share of other comprehensive income of associates (net of tax)	11,092	(15,815)
Actuarial gain/(loss) on retirement benefit obligation	(39,609)	22,339
Deferred tax effect on actuarial gain	15,805	(13,104)
Net other comprehensive income/(expenses) not to be reclassified to profit or loss in subsequent periods	797,100	(41,423)
Other comprehensive income/(expenses) for the year (net of tax)	797,100	(41,423)
Total comprehensive income/(expenses) for the year (net of tax)	1,411,243	330,285
Earnings per share		
Basic earnings per share (Rs.)	204.31	123.66
Diluted earnings per share (Rs.)	204.31	123.66
Dividend per ordinary share (Rs.)	-	20.00

STATEMENT OF FINANCIAL POSITION

As at 31st March	2021 Rs. '000	2020 Rs. '000
Assets		
Cash and cash equivalents	1,916,905	1,813,985
Placement with banks at Amortized cost	77,139	282,359
Financial investments - At FVOCI (quoted)	4,138,128	2,682,898
Financial investments - At FVPL	51,248	-
Loans and receivables at Amortized Cost	14,867,319	17,407,591
Finance leases receivables at Amortized Cost	14,221,461	13,746,155
Hire purchase receivables at Amortized Cost	649,866	1,605,426
Financial investments - at FVOCI (unquoted)	70,427	70,427
Other financial assets	423,949	438,638
Inventories	8,700	9,540
Other assets	225,526	45,984
Current tax refunds	79,130	146,042
Investment in associates	1,234,582	1,260,144
Investment property	237,381	246,166
Property, plant and equipment	3,279,866	3,105,781
Right-of-use assets	180,357	223,255
Leasehold property	40,270	40,739
Intangible assets	47,299	45,987
Total assets	41,749,548	43,171,119
Liabilities		
Bank overdraft	86,451	86,567
Deposits due to customers at Amortized Cost	23,060,274	22,814,923
Debt instruments issued and other borrowings at Amortized Cost	6,357,692	9,128,983
Other financial liabilities	552,252	855,247
Deferred tax liabilities	742,672	807,835
Other liabilities	82,704	54,865
Retirement benefit obligations	322,501	254,385
Lease Liability	235,431	269,986
Total liabilities	31,439,978	34,272,792
Shareholders' funds		
Stated capital	36,000	36,000
Revaluation reserve	2,589,864	2,325,585
Statutory reserve fund	796,400	761,400
General reserves	4,086,430	4,086,430
Retained earnings	2,723,183	2,016,150
Fair Value through OCI reserve	77,693	(327,238)
Total shareholders' funds	10,309,570	8,898,327
Total liabilities and shareholders' funds	41,749,548	43,171,119
Net assets per share (Rs.)	3,430	2,960

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/Senior General Manager

The Board of Directors are responsible for these Financial Statements. The Financial Statements were authorized for issue by the Directors on 31 May 2021. 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
31st May 2021

Shermal H. Jayasuriya
Finance Director

SELECTED KEY PERFORMANCE INDICATORS

Item	As at 31st March 2021		As at 31st March 2020	
	Actual	Required	Actual	Required
Regulatory Capital Adequacy				
Tier 1 Capital Adequacy Ratio	15.31%	6.50%	13.56%	6.50%
Total Capital Adequacy Ratio	17.07%	10.5%	15.25%	10.5%
Capital Funds to Deposit Liabilities Ratio	39.58	10.0%	35.31	10.0%
Quality of Loan Portfolio				
Gross Non-Performing Loans Ratio		14.13%		11.69%
Net-Non-Performing Loans Ratio		2.97%		3.22%
Net-Non-Performing Loans to Core Capital Ratio,		14.94%		19.23%
Provision Coverage Ratio,		61.99%		56.66%
Profitability				
Net Interest Margin		8.16%		9.71%
Return on Assets		1.98%		1.60%
Return on Equity		5.96%		4.18%
Cost to Income Ratio		72.34%		69.23%
Liquidity				
Available Liquid Assets to Required Liquid Assets (Minimum 100%)		283.25		264.64
Liquid Assets to External Funds		13.34		11.84
Memorandum information				
Number of Branches		39		39
External Credit Rating		Long-term Financial Institution Rating at BBB-(lka) (Negative outlook) by Fitch Ratings		Long-term Financial Institution Rating at BBB-(lka) (Negative outlook) by Fitch Ratings

CERTIFICATION:

We, the undersigned, being the Chief Financial Officer, Finance Director, Managing Director and the Compliance Officer of Mercantile Investments and Finance PLC certify jointly that:

- the above statements have been prepared in compliance with the format and definitions prescribed by the Central Bank of Sri Lanka (CBSL);
- the information contained in these statements have been extracted from the unaudited financial statements of the Licensed Finance Company unless indicated as audited.

Deva Anthony
Chief Financial Officer/
Senior General Manager

Ramidu Costa
Compliance Officer

Shermal Jayasuriya
Finance Director

Gerard Ondaatje
Managing Director